

## Tax Treatment of Payments Made on Behalf of, and Reimbursements Received by, Connecticut Homeowners Affected by Deteriorating Concrete Foundations Containing the Mineral Pyrrhotite

### Announcement 2020-5

This announcement addresses the Federal income tax treatment of financial assistance provided to Connecticut homeowners for the repair of deteriorating concrete foundations due to pyrrhotite. Pyrrhotite is a mineral that oxidizes in the presence of water and oxygen, leading to the formation of expansive mineral products. Pyrrhotite is naturally found in certain stone aggregates used to produce concrete and can cause concrete to deteriorate prematurely in certain cases.

In August 2015, agencies of the State of Connecticut began investigating numerous complaints by homeowners concerning the premature deterioration of the concrete foundations of their homes. These agencies concluded that the premature deterioration of the concrete foundations was due to the presence of pyrrhotite in the concrete mixture used to pour the foundations (deteriorating concrete foundations).

In response to the agencies' investigation, the State of Connecticut enacted legislation to allow a Connecticut resident owning a home with a concrete foundation the option to request a reassessment of the assessed value of the home based on a

written evaluation from a licensed engineer indicating the home had a deteriorating concrete foundation.

In 2017, the State of Connecticut mandated the establishment and funding of an entity, the Connecticut Foundation Solutions Indemnity Company, Inc. (CFSIC), to assist homeowners with the expeditious repair of the most severe cases of deteriorating concrete foundations. In addition to establishing the CFSIC, the State of Connecticut authorized the CFSIC to raise funds and augment the monies bonded by the state to remedy the issue of deteriorating concrete foundations.

In January 2019, the CFSIC began accepting applications from homeowners seeking financial assistance to repair their deteriorating concrete foundations. All claims require a contract between the homeowner and a contractor for repair or replacement of the foundation. The contract must set forth the total cost of repair. The CFSIC pays the lesser of: (1) the expenses pertaining to the repair of the crumbling foundation to a structurally safe level, or (2) \$175,000, per residential building. There are two types of claims that homeowners can make. The first type of claim requests that the CFSIC pay the contractor directly, on behalf of the homeowner, for eligible expenses before and during the performance of the repair work. The second type of claim requests that the CFSIC reimburse the homeowner directly for eligible expenses previously paid to the contractor. Payments under both types of claims commenced in 2019.

Guidance published in 2017 and 2018 by the Department of the Treasury and the Internal Revenue Service (IRS) provided a safe harbor that allows a homeowner, under

certain conditions, to treat amounts paid to repair damage to a personal residence with a deteriorating concrete foundation as a casualty loss under section 165 of the Internal Revenue Code (Code) so long as the taxpayer was not fully reimbursed by insurance or otherwise before filing a Federal income tax return for the year the loss was sustained. See Revenue Procedure 2017-60, 2017-50 I.R.B. 559; Revenue Procedure 2018-14, 2018-9 I.R.B. 378.

If a Connecticut homeowner who paid amounts to repair damage to a personal residence with a deteriorating concrete foundation has claimed a deduction under the safe harbor or otherwise on an original or amended Federal income tax return for an earlier taxable year, then payments received by the homeowner from the CFSIC in a subsequent taxable year must be included in the homeowner's gross income in the Federal income tax return for the subsequent taxable year to the extent the deduction claimed for the earlier taxable year resulted in a Federal income tax benefit. See section 111 of the Code. For example, if a homeowner claimed a deduction of \$125,000 for such amounts in an earlier taxable year and the entire deduction resulted in a reduction in Federal income tax from the tax that would apply without the deduction, a \$125,000 recovery must be included as gross income in the homeowner's Federal income tax return for the subsequent taxable year.

Existing guidance does not specifically address the Federal income tax treatment of a payment made by the CFSIC to a Connecticut homeowner who has not claimed a Federal income tax deduction for amounts paid to repair damage to a personal residence with a deteriorating concrete foundation.

If a Connecticut homeowner has not claimed a Federal income tax deduction for amounts paid to repair damage to a principal residence under the safe harbor or otherwise, or to the extent such a deduction did not result in a Federal income tax benefit, payments from the CFSIC to contractors (on behalf of the homeowner) or reimbursements paid to the homeowner will not be treated as includible in gross income of the homeowner in the year the payment or reimbursement is paid. Reimbursed repair costs cannot be deducted or included in the basis of a home.

For further information regarding this announcement, contact Martin Osborne of the Office of Associate Chief Counsel (Income Tax & Accounting) at (202) 317-7006 (not a toll-free call).