§ 1.1332–1

Inclusion in gross income of war loss recoveries.

(a) Amount of recovery. Except as provided in section 1333(1), the amount of the recovery in respect of a war loss in a previous taxable year is determined in the same manner for the purpose of either section 1332 or 1333. The amount of the recovery of any money or property in respect of any war loss is the aggregate of the amount of such money and of the fair market value of such property, both determined as of the date of the recovery. But see paragraph (a) of § 1.1333–1 for optional valuation where the taxpayer recovers the same war loss property.

(b) Amount of gain includible. (1) A taxpayer who has sustained a war loss described in section 127(a) of the Internal Revenue Code of 1939 and who has not elected to have the provisions of section 1333 apply to any taxable year in which he recovered any money or property in respect of a war loss in any previous taxable year must include in his gross income for each taxable year, to the extent provided in section 1332, the amount of his recoveries of money and property for such taxable year in respect of any war loss in a previous taxable year. Section 1332 provides that such recoveries for any taxable year are not includible in income until the taxpayer has recovered an amount equal to his allowable deductions in prior taxable years on account of such war losses which did not result in a reduction of any tax under chapter 1 or 2 of the Internal Revenue Code of 1939. War loss recoveries are considered as made first on account of war losses allowable but not actually allowed as a deduction, and second on account of war losses allowed as a deduction but which did not result in a reduction of tax under chapter 1 or 2 of the Internal Revenue Code of 1939. If there were deductions allowed on account of war losses for two or more taxable years which did not result in a reduction of any tax under chapter 1 or 2 of the Internal Revenue Code of 1939, a recovery on account of such losses is considered as made on account of such losses in the order of the taxable years for which they were allowed beginning with the latest. See § 1.1337–1 for the determination of the amount of such deductions. Recoveries in excess of such amount are treated as ordinary income until such excess equals the amount of the taxpayer’s allowable deductions in prior taxable years on account of war losses which did result in a reduction of any such tax under chapter 1 or 2 of the Internal Revenue Code of 1939. Any further recoveries in excess of all the taxpayer’s allowable deductions in prior taxable years for war losses are treated as gain on an involuntary conversion of property as a result of its destruction or seizure, and such gain is recognized or not recognized under the provisions of section 1033. See section 1033 and the regulations thereunder.

(2) The determination as to whether and to what extent any recoveries are to be included in gross income is made upon the basis of the amount of all the recoveries for each day upon which there are any such recoveries, as follows:

(i) The amount of the recoveries for any day is not included in gross income, and is not considered gain on an involuntary conversion, to the extent, if any, that the aggregate of the allowable deductions in prior taxable years on account of war losses which did not result in a reduction of any tax under the
taxpayer under chapter 1 or 2 of the Internal Revenue Code of 1939, as determined under §1.1337–1, exceeds the amount of all previous recoveries in the same and prior taxable years.

(ii) The amount of the recoveries for any day which is not excluded from gross income under subdivision (i) of this subparagraph is included in gross income as ordinary income, and is not considered gain on an involuntary conversion, to the extent, if any, that the aggregate of all the allowable deductions in prior taxable years on account of war losses (both those which resulted in a reduction of a tax of the taxpayer and those which did not) exceeds the sum of the amount of all previous recoveries in the same and prior taxable years and of that portion, if any, of the amount of the recoveries for such day which is not included in gross income under subdivision (i) of this subparagraph.

(iii) The amount of the recoveries for any day which is not excluded from gross income under subdivision (i) of this subparagraph and is not included in gross income as ordinary income under subdivision (ii) of this subparagraph is considered gain on an involuntary conversion of property as a result of its destruction or seizure. The following provisions then apply to this gain:

(a) Such gain is recognized or not recognized under the provisions of section 1033, relating to gain on the involuntary conversion of property. For the purpose of applying section 1033, such gain for any day is deemed to be expended in the manner provided in section 1033 to the extent the recovery for such day is so expended.

(b) If such gain is recognized, it is included in gross income as ordinary income or, if the provisions of section 1231(a) apply and require such treatment, as gain on the sale or exchange of a capital asset held for more than six months. For the purpose of applying section 1231(a), such recognized gain for any day is deemed to be derived from property described in that section to the extent of the recovery for such day with respect to such property, except such portion of such recovery as is attributable to the nonrecognized gain for such day.

(c) Section 1336 provides that in determining the unadjusted basis of recovered property, the total gain and the recognized gain with respect to such property must be determined. For such purpose, the recognized gain deemed to be derived from properties described in section 1231(a) may be allocated among such properties in the proportion of the recoveries with respect to such properties, reduced for each property by the portion of the recovery attributable to the nonrecognized gain for such day, and the recoveries with respect to properties not described in section 1231(a) may be similarly allocated. The total gain derived from any recovered property is the sum of the nonrecognized gain attributable to the recovery of such property and of the recognized gain allocable to such property.

(3) The foregoing provisions may be illustrated by the following examples:

Example 1. The taxpayer sustained war losses of $3,000 on account of properties A, B, C, and D. Of this amount, $1,000 did not result in a reduction of any income tax of the taxpayer, as determined under the provisions of §1.1337–1. In a subsequent taxable year, he received an award of $800 from the Government on account of property A. This is not included in income since it is less than the amount by which his allowable deductions for prior taxable years on account of war losses which did not result in any tax benefit ($1,000) exceed $0, the sum of all his previous recoveries. On a later date the taxpayer recovers property B, which is worth $1,500 on the date of recovery. This recovery is not included in gross income to the extent of $200, the amount by which the aggregate of the allowable deductions for prior taxable years on account of war losses which did not result in any tax benefit ($1,000) exceed $0. The remaining $1,300 of the recovery is included in gross income as ordinary income, and is not considered gain on the involuntary conversion of property, since it is less than the amount by which the aggregate of all the allowable deductions in prior taxable years on account of war losses ($3,000) exceeds $1,000, the sum of the $800 of previous recoveries and of the $200 portion of the recovery with respect to B which is not included in gross income. On a still later date the taxpayer sells for $2,500 his rights to recover C. Since the allowable deductions for prior taxable years on account of war losses which did not result in any tax benefit ($1,000) do not exceed the previous recoveries by the taxpayer ($800 and
§ 1.1333–1 26 CFR Ch. I (4–1–12 Edition)

$1,500, or $2,300), none of the recovery on account of C is excluded from gross income. This recovery is included in gross income as ordinary income, and is not considered gain on the involuntary conversion of property, to the extent of $700, the amount by which the aggregate of all the allowable deductions for prior taxable years on account of war losses exceeds $2,300, the sum of the $2,300 of previous recoveries and of the $0 portion of the recovery on account of C which is not included in gross income. Therefore, all of the $3,000 recognized gain would be subject to the provisions of section 1231(a).

(4) An allowable deduction with respect to a war loss is any deduction to which the taxpayer is entitled on account of any war loss property, regardless of whether or not such deduction was claimed by the taxpayer or otherwise allowed in computing his tax. If a deduction was claimed by a taxpayer in computing his tax for any taxable year and if such deduction was disallowed, such deduction will not be considered an allowable deduction for such taxable year since the previous determination will not be reconsidered.


§ 1.1333–1 Tax adjustment measured by prior benefits.

(a) Amount of recovery. The amount of recovery for purposes of this section shall be determined in accordance with the provisions of section 1332(a). See paragraph (a) of §1.1332–1. If, pursuant to the taxpayer’s election under section 1335, the provisions of section 1333 are applicable to any taxable year in which he recovers the same war loss property, the fair market value of such property shall, at the option of the taxpayer, be considered an amount equal to the adjusted basis (for determining loss) of such property in the hands of the taxpayer on the date such property was considered as destroyed or seized. This option is exercisable by the taxpayer with respect to each separate war loss property. Also, if the provisions of section 1333 are applicable pursuant to the taxpayer’s election, the amount of the recovery of any money or property in respect of war loss property shall be reduced for the purpose of section 1333 (2) and (3) by the amount of the obligations or liabilities with respect to such property, if the taxpayer for any previous taxable year chose under section 127(b)(2) of the Internal Revenue Code of 1939 to treat such obligations or liabilities as discharged or satisfied out of such property, and such obligations or liabilities were not so discharged or satisfied before the date of the recovery. See 26 CFR (1939) 29.127(b)–1 (Regulations 111).

(b) Elective method: tax adjustment measured by prior benefits. (1) If the taxpayer elects pursuant to section 1335