



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, DC 20224
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OFFICE OF
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MEMORANDUM FOR HARRY MARTIN
FED-STATE COORDINATOR, NORTH-SOUTH CAROLINA
DISTRICT

FROM: Lewis J. Fernandez
Deputy Assistant Chief Counsel
(Income Tax & Accounting)

SUBJECT: NORTH CAROLINA FLOOD RELIEF - INCOME
REPLACEMENT

This Technical Assistance is in response to your request for assistance dated December 15, 1999, regarding the tax treatment of state payments made to individuals and businesses of North Carolina who suffered losses due to the flood damage caused by Hurricane Floyd. Technical Assistance does not relate to a specific case and is not binding on examination or appeals. This document is not to be cited as precedent.

ISSUE:

Are the following flood relief payments gross income to the recipient upon which information reporting is required under § 6041 of the Internal Revenue Code: payments to farmers for crop yield losses; payments to farmer owned cooperatives for commodity quality losses; supplemental payments to growers' associations for uncollected assessments; and payments to fishermen for harvest losses?

CONCLUSION:

The following flood relief payments are gross income to the recipient upon which information reporting is required under § 6041: payments to farmers for crop yield losses; payments to farmer owned cooperatives for commodity quality losses; supplemental payments to growers' associations for uncollected assessments; and payments to fishermen for harvest losses.

FACTS:

The General Assembly of North Carolina declared Hurricane Floyd the worst natural disaster in the State's history. In the latter part of 1999, Hurricane Floyd caused

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extensive and prolonged flooding that devastated the civil, social, economic and environmental well-being of Eastern North Carolina. The entire economic base of Eastern North Carolina was undermined making it extremely difficult for individuals to earn income to support themselves and their families. In response to the widespread damage caused by Hurricane Floyd, Governor Jim Hunt, Jr. of North Carolina proposed a state emergency package that consisted of numerous relief programs to assist individuals and small businesses in recovering from the disaster. The "Hurricane Floyd Recovery Act of 1999," appropriating funds for a package of relief programs, was enacted on December 16, 1999.

The following disaster assistance programs are addressed in this Technical Assistance. The numbers appeared in the margin of materials in your request for assistance.

Crop Disaster Assistance (8)

This grant program provides payments of up to 17 percent of the yield losses suffered by farmers from the damage caused by Hurricane Floyd. These payments are in addition to the crop-loss disaster assistance provided by the federal government.

Commodity Quality Losses and Association Assessment Losses (11)

This grant program provides supplemental payments to farmer-owned cooperatives for quality losses associated with flood-damaged commodities. These cooperatives purchased commodities that have been found to be deficient in quality due to damage associated with the flooding. The payments under this program will indemnify the cooperatives for losses caused by quality deficiencies.

Additionally, this program provides supplemental payments to growers' associations for uncollected assessments. Many of these associations operate on an assessment per harvested acre basis to fund promotion and marketing of individual North Carolina commodities. Because the floods prevented the harvest of these critical products, the Associations are unable to provide the necessary marketing assistance to maintain demand.

Commercial Fishing Disaster Assistance (12)

This fishing loss disaster assistance program provides North Carolina fishermen with grants and loans to compensate them for loss of income due to harvest losses caused by the flooding. The North Carolina Division of Marine Fisheries will verify losses based on historical fishing activity.

The Hurricane Floyd Recovery Act of 1999, 1999 N.C. Sess. Laws 1999-463 Extra Session, § 4.5, requires that State agencies distributing the funds inform recipients by written statement of the federal and State income tax consequences of the

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disbursements. In response to this requirement, the North Carolina Department of Revenue has requested your assistance in determining the federal income tax treatment of the disbursements.

LAW AND ANALYSIS:

Section 61(a) provides generally that gross income means all income from whatever source derived. Section 1.61-1(a) of the Income Tax Regulations provides that gross income includes income realized in any form. In Commissioner v. Glenshaw Glass Co., 348 U.S. 426 (1955), 1955-1 C.B. 207, the United States Supreme Court held that the concept of gross income encompassed accessions to wealth, clearly realized, over which taxpayers have complete dominion.

The Crop Disaster Assistance program, Commodity Quality Loss and Association Assessment Loss programs, and the Commercial Fishing Disaster Assistance program provide grants for crop yield losses, fish harvest losses, commodity quality losses and assessment association losses. These grants would clearly be income subject to federal tax had they been profits generated in the normal course of business. Thus, the payments made under these supplemental grant programs to reimburse taxpayers for their lost profits constitute gross income to the recipients within the meaning of § 61 (unless the payment is a loan rather than a grant).

Section 6041(a) provides that all persons engaged in a trade or business and making payment in the course of such trade or business to another person of rent, salaries, wages, premiums, annuities, compensations, remunerations, emoluments or other fixed or determinable gains, profits, and income of \$600 or more in any taxable year shall render a true and accurate return to the Secretary of the Treasury, under such regulations and in such form and manner and to such extent as may be prescribed, setting forth the amount of such gains, profits and income, and the name and address of the recipient of such payment. Under § 1.6041-1(b), federal and state governments are considered persons engaged in a trade or business for purposes of § 6041. Additionally, under § 1.6041-3(c), payments to a corporation are generally exempt from the information reporting requirements.

The grant programs described in this Assistance provide for payments that are “fixed or determinable gains, profits or income,” to the recipients. Thus, information reporting is required under § 6041 unless the payments are made to incorporated entities.

Accordingly, we suggest that you advise the State of North Carolina that, subject to the exceptions, information reporting is required on grants to farmers for crop yield losses, on grants to farmer owned cooperatives for commodity losses, on grants to growers’ associations for assessment losses, and on grants to commercial fishermen for harvest losses. Further, we suggest that you advise the State of North Carolina to describe the

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tax consequences of these grants to the recipients in language similar to the following:

The Internal Revenue Service has advised us that you must include in income any crop insurance proceeds you receive as the result of crop damage. You generally include them in the year you receive them. Treat as crop insurance proceeds the crop disaster payments or other payments you receive from the state or federal government as the result of destruction or damage to crops, or the inability to plant crops, or lost fishing income, because of drought, flood, or any other natural disaster (unless the payment is a loan rather than a grant). Information may also be found in IRS Publication 225, Farmer's Tax Guide.

Taxpayers uncertain whether these principles or interpretations of tax law should apply to their situations should consider seeking a private letter ruling or, if appropriate, technical advice. Procedures for issuing letter rulings and technical advice are in Rev. Proc. 2000-1, 2000-1 I.R.B. 4, and Rev. Proc. 2000-2, 2000-1 I.R.B. 73, respectively.

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If you have further questions about this memorandum, please call George Baker at (202) 622-4920.