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Drought Disaster Overview

Jim R. Barbee

From: Yezak, Jennifer - OSEC [Jennifer.Yezak@osec.usda.gov]
Sent: Monday, July 23, 2012 8:24 AM
To: Yezak, Jennifer - OSEC
Cc: Wyant, Monica - OSEC; Griffis, Janice - OSEC
Subject: Agriculture Secretary Vilsack Announces New Obama Administration Efforts to Assist Farmers and Ranchers Impacted by Drought

News Release **Embargoed until 11:45 am eastern time**

Good morning,

Below is a news release announcing new flexibility and assistance in USDA's major conservation programs and plans to encourage crop insurance companies to provide a short grace period for farmers on unpaid insurance premiums. Please keep the news release embargoed until 11:45 am today. If you have any questions, please contact me.

Best regards,
Jennifer
202-205-9994

Embargoed until 11:45 am eastern time

Agriculture Secretary Vilsack Announces New Obama Administration Efforts to Assist Farmers and Ranchers Impacted by Drought

WASHINGTON, July 23, 2012-Agriculture Secretary Tom Vilsack today announced new flexibility and assistance in the U.S. Department of Agriculture's major conservation programs to get much-needed help to livestock producers as the most wide-spread drought in seven decades intensifies in the United States. Vilsack also announced plans to encourage crop insurance companies to provide a short grace period for farmers on unpaid insurance premiums, as some farming families can be expected to struggle to make ends meet at the close of the crop year.

"President Obama and I are committed to getting help to producers as soon as possible and sustaining the success of America's rural communities through these difficult times," said Vilsack. "Beginning today, USDA will open opportunities for haying and grazing on lands enrolled in conservation programs while providing additional financial and technical assistance to help landowners through this drought. And we will deliver greater peace of mind to farmers dealing with this worsening drought by encouraging crop insurance companies to work with farmers through this challenging period. As severe weather and natural disasters continue to threaten the livelihoods of thousands of our farming families, we want you and your communities to know that USDA stands with you."

The assistance announced uses the Secretary of Agriculture's existing authority to help create and encourage flexibility within four USDA programs: the Conservation Reserve Program (CRP), the Environmental Quality Incentives Program (EQIP), the Wetlands Reserve Program (WRP), and the Federal Crop Insurance Program.

Conservation Reserve Program (CRP)
To assist farmers and ranchers affected by drought, Vilsack is using his discretionary authority to allow additional acres under CRP to be used for haying or grazing under emergency conditions. CRP is a voluntary program that provides producers annual rental payments on their land in exchange for planting resource conserving crops on cropland to help prevent erosion, provide wildlife habitat and improve the environment. CRP acres can already be used for emergency haying and grazing during natural disasters to provide much needed feed to livestock. Given the widespread nature of this drought, forage for livestock is already substantially reduced. The action today will allow lands that are not yet classified as "under severe drought" but that are "abnormally dry" to be used for haying and grazing. This will increase available forage for livestock. Haying and grazing will only be allowed following the local primary nesting season, which has already passed in most areas. Especially sensitive lands such as wetlands, stream buffers and rare habitats will not be eligible.

Environmental Quality Incentives Program (EQIP)
To assist farmers and ranchers affected by drought, Vilsack is using his discretionary authority to provide assistance to farmers and ranchers by allowing them to modify current EQIP contracts to allow for prescribed grazing, livestock watering facilities, water conservation and other conservation activities to address drought conditions. EQIP is a voluntary program that provides financial and technical assistance to agricultural producers on their land to address natural resource concerns on agricultural and forest land. The USDA Natural Resources Conservation Service (NRCS) will work closely with producers to modify existing EQIP contracts to ensure successful implementation of planned conservation practices. Where conservation activities have failed because of drought, NRCS will look for opportunities to work with farmers and ranchers to re-apply those activities. In the short term, funding will be targeted towards hardest hit drought areas.

Wetlands Reserve Program (WRP)
To assist farmers and ranchers affected by drought, Vilsack is using his discretionary authority to authorize haying and grazing of WRP easement areas in drought-affected areas where such haying and grazing is consistent with conservation of wildlife habitat and wetlands. WRP is a voluntary conservation easement program that provides technical and financial assistance to agricultural producers to restore and protect valuable wetland resources on their property. For producers with land currently enrolled in WRP, NRCS has expedited its Compatible Use Authorization (CUA) process to allow for haying and grazing. The compatible use authorization process offers NRCS and affected producers with the management flexibility to address short-term resource conditions in a manner that promotes both the health of the land and the viability of the overall farming operation.

Federal Crop Insurance Program
To help producers who may have cash flow problems due to natural disasters, USDA will encourage crop insurance companies to voluntarily forego charging interest on unpaid crop insurance premiums for an extra 30 days, to November 1, 2012, for spring crops. Policy holders who are unable to pay their premiums in a timely manner accrue an interest penalty of 1.25 percent per month until payment is made. In an attempt to help producers through this difficult time, Vilsack sent a letter to crop insurance companies asking them to voluntarily defer the accrual of any interest on unpaid spring crop premiums by producers until November. In turn, to assist the crop insurance companies, USDA will not require crop insurance companies to pay uncollected producer premiums until one month later.

Thus far in 2012, USDA has designated 1,297 counties across 29 states as disaster areas, making all qualified farm operators in the areas eligible for low-interest emergency loans. Increasingly hot and dry conditions from California to Delaware have damaged or slowed the maturation of crops such as corn and soybeans, as well as pasture- and range-land. Vilsack has instructed USDA subcabinet leaders to travel to affected areas to augment ongoing assistance from state-level USDA staff and provide guidance on the department's existing disaster resources. To deliver assistance to those who need it most, the Secretary recently reduced the interest rate for emergency loans from 3.75 percent to 2.25 percent, while lowering the reduction in the annual rental payment to producers on CRP acres used for emergency haying or grazing from 25 percent to 10 percent. Vilsack has also simplified the Secretarial disaster designation process and reduced the time it takes to designate counties affected by disasters by 40 percent.

USDA agencies have been working for weeks with state and local officials, as well as individuals, businesses, farmers and ranchers, as they begin the process of helping to get people back on their feet. USDA offers a variety of resources for states and individuals affected by the recent disasters. For additional information and updates about USDA's efforts, please visit www.usda.gov/drought.

The Obama Administration, with Agriculture Secretary Vilsack's leadership, has worked tirelessly to strengthen rural America, maintain a strong farm safety net, and create opportunities for America's farmers and ranchers. U.S. agriculture is currently experiencing one of its most productive periods in American history thanks to the productivity, resiliency, and resourcefulness of our producers. A strong farm safety net is important to sustain the success of American agriculture. USDA's crop insurance program currently insures 264 million acres, 1.14 million policies, and $110 billion worth of liability on about 500,000 farms. In response to tighter financial markets, USDA has expanded the availability of farm credit, helping struggling farmers refinance loans. In the past 3 years, USDA provided 103,000 loans to family farmers totaling $14.6 billion. Over 50 percent of the loans went to beginning and socially disadvantaged farmers and ranchers.

Embargoed until 11:45 am eastern time

Jennifer Yezak
Director, Office of External and Intergovernmental Affairs
U.S. Department of Agriculture
202.205.9994 (direct) / 202-255-7061 (cell)

Jim R. Barbee

From: Koble, Clinton - FSA, Reno, NV [clinton.koble@nv.usda.gov]
Sent: Friday, July 20, 2012 3:32 PM
To: Allison Copening ; Barbara K. Cegavske ; Ben Kieckhefer ; David R. Parks ; Dean A. Rhods ; Don Gustavson ; Greg Brower ; James A. Settelmeyer ; John J. Lee ; Joseph P. Hardy MD ; Mark Manendo ; Michael A. Schneider ; Michael Roberson ; Mike McGinness ; Mo Denis ; Ruben Kihuen ; Shirley A. Breeden ; Steven A. Horsford ; Valerie Wiener; April Mastroluca ; Cresent Hardy ; David Bobzien ; Debbie Smith ; Dina Neal ; Ed Goedhart ; Elliot T. Anderson ; Harvey J. Munford ; Ira Hansen ; Irene Bustamante-Adams; James Ohrenschall ; Jason Frierson ; John Ellison ; John Hambrick ; John Oceguera ; Joseph M. Hogan ; Kelly Kite ; Kelvin Atkinson ; Lucy Flores ; Lynn D. Stewart ; Maggie Carlton ; Marcus Conklin ; Marilyn Dondero-Loop ; Marilyn Kirkpatrick ; Mark Sherwood ; Melissa Woodbury ; Olivia Diaz ; Pat Hickey ; Paul Aizley; Peggy Pierce ; Pete Goicoechea ; Pete Livermore ; Randy Kirner ; Richard (Skip) Daly ; Richard Carrillo ; Richard McArthur ; Scott Hammond ; Steven Brooks ; Teresa Benitez-Thompson; Tick Segerblom ; Tom Grady ; William Horne
Cc: cbsmith@dps.state.nv.us; Lucas Foletta; Jim R. Barbee
Subject: URGENT: Update on the Secretarial Drought Declaration
Importance: High

Ladies and Gentlemen of the Nevada State Legislature:

Below is an important update on the Secretarial Drought Declaration and the many ramifications and resources due to this Declaration. Please distribute to any constituent that may want or need this information. Feel free to contact me at the information posted below if you have additional questions.

Please make note of the important link posted in the next to last paragraph below for the USDA's Drought Page (www.usda.gov/drought) then scroll to the bottom and under 'Disaster Declarations – What and Where are They', click on DisasterAssistance.gov; that page provides information on all available federal assistance.

Clint Koble, State Executive Director
Farm Service Agency
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"Team USDA: Revitalizing rural America every day in every way"
Know Your Farmer, Know Your Food!

From: National Office Communications
Sent: Friday, July 20, 2012 7:31 AM
To: FAS.1-All FAS Washington; FAS.1-AllFASOverseas; ug-AGCENTRAL-allfac; ug-AGEAST-allfac; ug-AGLO-allfac; ug-AGWEST-allfac; ug-its; ASOC-ALL
Subject: FW: An Update on the Drought

From: The Office of the Secretary - OSEC
Sent: Friday, July 20, 2012 10:30:25 AM (UTC-05:00) Eastern Time (US & Canada)
To: WCTS - ALL-USDA-2K
Subject: An Update on the Drought

UNITED STATES DEPARTMENT OF AGRICULTURE
OFFICE OF THE SECRETARY
WASHINGTON, D.C. 20250

Dear USDA Employees,

This week, President Obama asked me to brief him on the historic drought currently impacting much of the country. Today I want to take this opportunity to update you as well, on where we stand right now and on our ability to help folks who are impacted around the country.

First, I want to recognize many of you whose farms and ranches – or those of your family, friends and neighbors – are impacted by this disaster. Your ongoing commitment to deliver services, advice and information to your communities in this difficult time is invaluable, and you are in my thoughts every day.

Like all weather events, this drought remains unpredictable – but we do know that it's one of the worst in history. To date, USDA has designated 1,055 counties in 26 states as disaster areas due to drought. Thursday's Drought Monitor report shows that 88 percent of our nation's corn and 87 percent of our soybeans are impacted, and this week's meteorological reports show that many areas of the country can continue to expect hot, dry weather in the short term.

Last week, I made three announcements that will allow us to deliver better service to producers.

- I announced a final rule to simplify the process for Secretarial disaster designations – both for producers and for State government officials. The streamlined disaster designation process has helped us respond to drought more quickly.

- USDA reduced the interest rate for FSA Emergency Loans, effectively lowering the current rate from 3.75 percent to 2.25 percent.

- Finally, we have lowered the payment reduction for Conservation Reserve Program (CRP) lands that qualify for emergency haying and grazing in 2012, from 25 to 10 percent. This means a smaller burden on livestock operators who desperately need land to graze.

Meanwhile, as you know, our authority to take further action is limited because the disaster programs in the 2008 Farm Bill expired last year. This is why we continue to call on Congress to act, to ensure we have the tools to help farm families during a time of significant drought.

As we continue doing all we can to help producers and families impacted by this drought, USDA has set up a special web page to deliver the most up-to-date information possible. I encourage you to visit USDA's Drought Page (www.usda.gov/drought), which in addition to news contains a number of fact sheets and information that can be shared with producers.

With your help, USDA will carry out President Obama's direction to do all we can in support of farmers and ranchers – and we'll help American agriculture carry on as strong as ever.

Sincerely,
Secretary Tom Vilsack

USDA FSA

FACT SHEET

UNITED STATES DEPARTMENT OF AGRICULTURE
FARM SERVICE AGENCY

July 2012

Emergency Disaster Designation and Declaration Process

Overview

Agriculture-related disasters and disaster designations are quite common. One-half to two-thirds of the counties in the United States have been designated as disaster areas in each of the past several years, even in years of record crop production.

The Secretary of Agriculture is authorized to designate counties as disaster areas to make emergency loans (EM) to producers suffering losses in those counties and in counties that are contiguous to a designated county. In addition to EM eligibility, other emergency assistance programs, such as FSA disaster assistance programs, have historically used disaster designations as an eligibility requirement trigger.

The Farm Service Agency (FSA) streamlined the USDA Disaster Designation process to make assistance more readily available and with less burdensome paperwork.

Types of Disaster Designations

FSA administers four types of disaster designations:

- USDA Secretarial disaster designation (This designation is most widely used).
- Presidential major disaster and Presidential emergency declarations,
- FSA Administrator's Physical Loss Notification and,
- Quarantine designation by the Secretary under the Plant Protection Act or animal quarantine laws as defined in § 2509 of the Food, Agriculture, Conservation and Trade Act of 1990 (mentioned in 7 CFR part 761, which includes a definition of "quarantine" in accordance with 7 U.S.C. 1961).

What Does a Disaster Designation Specify?

A disaster designation specifies:

- The disaster that resulted in the designation;
- The incidence period (dates) of that disaster;
- The specific counties included in the designation.

Procedures for Severe Drought

The streamlined process provides for nearly an automatic designation for any county in which drought conditions, as reported in the U.S. Drought Monitor (http://droughtmonitor.unl.edu/) when any portion of a county meets the D2 (Severe Drought) drought intensity value for eight consecutive weeks. A county that has a portion of its area in a drought intensity value of D3 (Extreme Drought) or higher at any time during the growing season also would be designated as a disaster area.

Benefits of the Streamlined Disaster Designation Process

The new process helps reduce paperwork and documentation requirements at the local FSA level, making the process more efficient and timely. Individual producer losses would still need to be documented for Emergency Loan (EM) Program eligibility.

Highlights of the New Rule Governing Secretarial Disaster Designations

- The new rule governing disaster designations:
  - Streamlines the USDA Secretarial designation process by eliminating steps from the current process;
  - Preserves the ability of a state governor or Indian Tribal Council to request a Secretarial Disaster Designation;
  - Removes the requirement that a request for a disaster designation be initiated only by a state governor or Indian Tribal Council;
  - Further streamlines the disaster designation process for severe drought occurrences by utilizing the U.S. Drought Monitor as a tool to automatically trigger disaster areas with no further documentation;
  - Does not impose any new requirements on producers or the public.

- For all other natural disaster occurrences and those drought conditions that are not considered severe, the county must either show a 30 percent production loss of at least one crop or a determination must be made by surveying producers that other lending institutions will not be able to provide emergency financing.

Location of Regulation Governing Disaster Designation Process

The rule is contained in the Federal Register dated July 13, 2012, at http://www.gpo.gov/fdsys/pkg/FR-2012-07-13/pdf/2012-17137.pdf168/77.

FACT SHEET

UNITED STATES DEPARTMENT OF AGRICULTURE
FARM SERVICE AGENCY

July 2012

Emergency Loan Program

Overview

USDA's Farm Service Agency (FSA) provides emergency loans to help producers recover from production and physical losses due to drought, flooding, other natural disasters or quarantine.

Loan Uses

Emergency loan funds may be used to:

- Restore or replace essential property;
- Pay all or part of production costs associated with the disaster year;
- Pay essential family living expenses;
- Reorganize the farming operation and;
- Refinance certain debts.

Eligibility

Emergency loans may be made to farmers and ranchers who:

- Own or operate land located in a county declared by the President or designated by the Secretary of Agriculture as a primary disaster area or quarantine area. All counties contiguous to the declared, designated, or quarantined primary counties also are eligible for emergency loans. A disaster designation by the FSA administrator authorizes emergency loan assistance for physical losses only in the designated and contiguous counties;
- Are established family farm operators and have sufficient farming or ranching experience;
- Are citizens or permanent residents of the United States;
- Have suffered at least a 30 percent loss in crop production or a physical loss to livestock, livestock products, real estate or chattel property;
- Have an acceptable credit history;
- Are unable to receive credit from commercial sources;
- Can provide collateral to secure the loan and;
- Have repayment ability.

Loan Requirements

FSA loan requirements are different from those of other lenders. Some of the more significant differences are the following:

- Borrowers must keep acceptable farm records;
- Borrowers must operate in accordance with a farm plan they develop and agree to with local FSA staff and;
- Borrowers may be required to participate in a financial management training program and obtain crop insurance.

Collateral is Required

All emergency loans must be fully collateralized. The specific type of collateral may vary depending on the loan purpose, repayment ability and the individual circumstances of the applicant. If applicants cannot provide adequate collateral, their repayment ability may be considered as collateral to secure the loan. A first lien is required on property or products acquired, produced or refinanced with loan funds.

Loan Limit

Producers can borrow up to 100 percent of actual production or physical losses, to a maximum amount of $500,000.

Loan Terms

Loans for crop, livestock, and non-real estate losses are normally repaid within one to seven years, depending on the loan purpose, repayment ability and collateral available as loan security. In special circumstances, terms of up to 20 years may be authorized. Loans for physical losses to real estate are normally repaid within 30 years. In certain circumstances, repayment may be made over a maximum of 40 years.

Interest Rate

The current annual interest rate for emergency loans is 2.25 percent.

Application Deadline

Applications for emergency loans must be received within eight months of the county's disaster or quarantine designation date.

Jim R. Barbee

From: Yezak, Jennifer - OSEC [Jennifer.Yezak@osec.usda.gov]
Sent: Monday, July 23, 2012 11:41 AM
To: 'Ryan McGinness'; Jim R. Barbee
Cc: Wyant, Monica - OSEC
Subject: Question regarding the IRS
Attachments: Notice 89-55.mht

Hello Ryan and Jim,

This is to follow up on your question about the IRS and the treatment of capital gains from livestock herd liquidations as a result of a natural disaster. In brief, IRS will accept the Secretarial disaster designations and allow producers to defer the capital gains from the liquidation of livestock due to natural disaster and there is a federal emergency designation. No further action by the local governments is necessary.

Specifically, the third paragraph of section III of Notice 89-55, which is attached, provides the details. The designation can be made by the President, or by a department or agency of the federal government. The notice specifically provides that designations made by USDA or its agencies are sufficient designations.

If you have any further questions, feel free to contact me or Monica.

Thanks,
Jennifer

Jennifer Yezak
Director, Office of External and Intergovernmental Affairs
U.S. Department of Agriculture
202.205.9994 (direct) / 202-255-7061 (cell)

Notice 89-55; 1989-1 C.B. 696;
*1989 IRB LEXIS 214, *; 1989-20 I.R.B. 134*

Notice 89-55

Notice 89-55; 1989-1 C.B. 696; 1989 IRB LEXIS 214; 1989-20 I.R.B. 134

January 1989

[*1]

SUBJECT MATTER: Year of Inclusion - Income Received on Account of Drought

TEXT:

The purpose of this notice is to provide guidance to farmers regarding the tax treatment of certain income received on account of drought.

I. Background

Section 451 of the Internal Revenue Code provides rules that govern the proper taxable year in which to include items in gross income. Generally, income is reported in the year it is received unless, under the method of accounting used to compute taxable income, the item is properly includible in another taxable year. However, section 451 also contains special rules permitting deferrals of income for certain amounts received by farmers for crops and livestock because of natural disaster and drought.

Specifically, section 451 (d) of the Code allows taxpayers, in certain circumstances, to defer the reporting of insurance proceeds received as a result of the destruction of or damage to crops. Similarly, section 451 (e) allows taxpayers to defer the reporting of income derived from the sale of livestock sold on account of drought, if certain requirements are met. Alternatively, section 1033 (e) allows for nonrecognition of the gain realized on the sale of livestock sold solely on account **[*2]** of drought if the livestock are replaced and the requirements of section 1033 are met.

The Disaster Assistance Act of 1988 (Pub. L. No. 100-387, 102 Stat. 924), in part, provides for payments to farmers affected by drought. Under Title I of the Act, livestock producers may receive assistance in the form of cash reimbursements for feed and certain transportation expenses, and in the form of donations and below market purchases of feed. Under Title II of the Act, crop producers may receive payments for destroyed or damaged crops. Section 321 of Title III of the Act provides, in effect, for cost-sharing payments for approved conservation practices.

This notice explains the extent to which payments under the Disaster Assistance Act of 1988 and certain other income recognized on account of drought qualify for deferral under sections 451 (d) and 451 (e) of the Code. This notice also addresses the proper tax treatment of payments and other benefits received under the Act.

II. Crop Loss Assistance

Section 451 (d) of the Code and section 1.451-6 of the Income Tax Regulations allow a taxpayer on the cash receipts and disbursements method of accounting who receives insurance proceeds for the destruction **[*3]** of or damage to crops to elect to include such proceeds in income for the taxable year following the year of destruction or damage if the taxpayer establishes that, under its normal business practice, income from the crops would have been reported in a year following the year of destruction or damage.

In order for a payment to constitute insurance for the destruction of or damage to crops, the insured must suffer actual loss. Agreements with insurance companies that provide for payments without regard to actual losses of the insured, *e.g.,* in the event that certain weather conditions occur or do not occur, do not constitute insurance payments for the destruction of or damage to crops. Accordingly, payments under such contracts will not qualify for deferral under section 451 (d) of the Code.

Under section 451 (d) of the Code, certain government payments for crop damage are treated as insurance proceeds. Specifically, payments received under the Agricultural Act of 1949 (as amended) for the destruction of or damage to crops caused by drought, flood, or other natural disaster, or the inability to plant crops because of such a natural disaster, will be treated as insurance proceeds received **[*4]** for the destruction of or damage to crops. Further, section 6033 of the Technical and Miscellaneous Revenue Act of 1988 (Pub. L. No. 100-647, 102 Stat. 3342) amended section 451 (d) to provide that payments received under Title II of the Disaster Assistance Act of 1988 as compensation for the destruction of or damage to crops, or the inability to plant crops, because of drought or any other natural disaster shall also be treated as insurance proceeds received as a result of the destruction of or damage to crops. Therefore, these payments may qualify for deferral under section 451 (d).

Title II of the Disaster Assistance Act of 1988 establishes disaster payment programs for eligible farmers that, as a result of drought, hail, or related condition in 1988, are unable to harvest sufficient quantities of various crops. Accordingly, a cash method taxpayer may elect to include in gross income for 1989 such Title II payments that are received in 1988, if the taxpayer establishes that, under its normal business practice, the income from such crops would have been included in its gross income for any taxable year following 1988. All Title II payments are eligible for this elective deferral under **[*5]** section 451 (d) of the Code, regardless of whether they are received before or after November 11, 1988, the date of enactment of the Technical and Miscellaneous Revenue Act of 1988.

A taxpayer must make an affirmative election to defer recognition of eligible payments under section 451 (d) of the Code. A taxpayer receiving multiple eligible payments that are attributable to a single trade or business must treat those amounts in a consistent manner, either including the amounts in income in the year of receipt or electing to include the amounts in income in the year following the year of destruction or damage. The time and manner of making the election were not changed by the Technical and Miscellaneous Revenue Act of 1988 and are set forth in section 1.451-6 (b) of the regulations. These rules are also generally explained in Publication 225, *Farmer's Tax Guide.* Rev. Rul. 74-145, 1974-1 C.B. 113, also provides guidance as to the manner of making this election. This election may also be made on an amended return.

III. Gain from the Sale or Exchange of Livestock

Section 451 (e) of the Code and section 1.451-7 of the regulations allow a cash method taxpayer, whose principal trade or business **[*6]** is farming, to elect to defer for one year gain realized from the sale of livestock solely on account of drought. The amount of income that may be deferred is the income attributable to the excess of the number of livestock sold or exchanged over the number that would have been sold, following usual business practices, in the absence of a drought. See section 1.451-7 (a) of the regulations for details of this computation.

The Technical and Miscellaneous Revenue Act of 1988 extends this one-year elective deferral to the gain realized from sales after December 31, 1987, of livestock held for draft, breeding, dairy, or sporting purposes regardless of the period of time that the livestock have been held. Before this change, a producer could not defer the gain realized from such sales if the livestock had been held for these purposes for 12 months or more (24 months in the case of cattle and horses).

For the sale to qualify under section 451 (e) of the Code, the drought that caused the sale must have resulted in an area being designated as eligible for assistance by the Federal Government. The designation may be made by the President or by an agency or department of the Federal Government. **[*7]** Determinations by the Department of Agriculture or agencies within the Department of Agriculture, such as the Farmer's Home Administration or the Agriculture Stabilization and Conservation Service, are sufficient designations. Similarly, determinations by other federal agencies such as the Federal Emergency Management Agency or the Small Business Administration also satisfy the requirement.

The livestock may be sold before an area is designated as eligible for federal assistance so long as the drought that caused the sale also caused the area to be so designated. Evidence must be submitted, pursuant to section 1.451-7 (g) of the regulations, explaining the relationship of the designated drought area to the taxpayer's early sale of the livestock.

To qualify for the one-year elective deferral, the livestock need not be raised, and the sale need not take place, in a drought area. The sale must occur, however, solely on account of drought conditions in the designated area, the existence of which affected the water, grazing, or other requirements' of the livestock so as to necessitate the sale. This requirement generally will not be met if the costs of food, water, or other requirements of **[*8]** the livestock affected by the drought are not substantial in relation to the total costs of holding the livestock.

As an alternative to the one-year deferral of gain under section 451 (e) of the Code, a producer may be eligible to defer gain under section 1033 (e). Under the rules of section 1033, a taxpayer that disposes of an asset in an involuntary conversion and replaces it in a timely manner with qualifying replacement property may defer the gain from the involuntary conversion until the replacement property is disposed of. Section 1033 (e) treats as an involuntary conversion the sale of livestock (other than poultry) held by a taxpayer for draft, breeding, or dairy purposes in excess of the number that the taxpayer would sell under usual business practices if such livestock is sold by the taxpayer solely on account of drought. Accordingly, the taxpayer may elect not to recognize the gain realized on the sale of the excess livestock if qualifying replacement property is purchased in a timely manner and the other requirements of section 1033 are met.

For details concerning other income eligible for deferral and for general information on other tax issues affecting farmers, see Publication **[*9]** 225, *Farmer's Tax Guide.*

IV. Treatment of Feed Assistance, Payments and Other Benefits

Title I of the Disaster Assistance Act of 1988 authorizes programs to provide feed assistance, reimbursement payments, and other benefits to qualifying livestock producers if, because of a natural disaster (such as drought, fire, hurricane, or earthquake), the Secretary of Agriculture determines that a livestock emergency exists. These programs include partial reimbursement for expenses incurred in purchasing feed and for certain transportation expenses, and the donation or sale at a below market price of feed owned by the Commodity Credit Corporation.

Title I payments are not proceeds from the sale of livestock and are not eligible for deferral under section 451 (e) of the Code. Similarly, Title I payments are not eligible for deferral under section 451 (d), which allows a one-year deferral for certain payments received for the destruction of or damage to crops raised by a taxpayer for sale, or for the inability to plant such crops because of a natural disaster. Although some Title I payments may be received for the loss of feed produced by a farmer for such farmer's livestock, no Title I payments **[*10]** are received for the destruction of or damage to crops raised for sale, or the inability to plant such crops. Thus, Title I payments are hot compensation for the loss of crops the income from which would have been reported in a later taxable year and are not eligible for deferral under section 451 (d).

In general, the reimbursement payments under Title I programs are includible in gross income in accordance with the recipient's method of accounting. A limited exception applies in the case of a taxpayer on the cash receipts and disbursements method of accounting whose application for reimbursement is approved prior to paying an expense that would be currently "deductible under section 162 of the Code. Under these circumstances, a taxpayer is not required to include the reimbursement payment in gross income; the deduction for the expense, however, is limited to the amount that is not reimbursed. *See* Rev. Rul. 79-263, 1979-2 C.B. 82. In other circumstances, the reimbursement payment is includible in gross income, and the deduction for the expense is not so limited.

Donations and below market sales of feed under Title I are not arm's length transactions; the purpose of the programs is to **[*11]** confer relief benefits on the recipients and purchasers. Accordingly, the market value of donated feed is includible in gross income in accordance with the recipient's method of accounting. Similarly, a purchaser of feed at below market prices must include in gross income the difference between the price paid and the market value of the feed. In either case, however, a deduction is allowable for the market value of the feed to the extent that the farmer would have been permitted to deduct currently the cost of purchasing the feed at market value. *Cf.* Rev. Rul. 73-13, 1973-1 C.B. 42. Thus, to the extent that the farmer is permitted a current deduction for the purchase of the feed, inclusion of the value of the conferred benefit in the farmer's income is offset by a current deduction and has no tax effect other than increasing the amount of the gross receipts from farming. If, on the other hand, the farmer would have been required to capitalize the cost of purchased feed, the value of the donated feed or the amount of the price reduction must also be capitalized.

Treatment of these benefits in this manner is consistent with the treatment of cost-sharing payments under other government **[*12]** programs. For example, cost-sharing payments under a government conservation, restoration, or reclamation program are generally includible in gross income unless the program is specified in section 126 of the Code, in which case a recipient may exclude all or a portion of the payments. If payments are not excluded from gross income under section 126, a taxpayer is treated as paying or incurring a cost equal in amount to the payment and may recover this cost through deduction, or through depreciation, cost of goods sold, depletion, or amortization (as in the case of a capitalized cost), to the extent provided for in the Code. *See* Rev. Rul. 84-67, 1984-1 C.B. 28.

Prior to the Disaster Assistance Act of 1988, owners and operators of farms and ranches may have entered into contracts with the Secretary of Agriculture (under subtitle D of title XII of the Food Security Act of 1985, 16 U.S.C. 3831 *et seq.*) to devote croplands normally used for agricultural production to a less intensive use, such as pasture or permanent grass. In return, the owner or operator receives rental payments as compensation for devoting the land to a less intensive use. In an emergency, such as a drought, the Secretary **[*13]** may authorize the harvesting of the croplands that are subject to these contracts, in which case the rental payments for the harvested land are reduced.

Section 321 of Title III of the Disaster Assistance Act of 1988 provides that, with respect to any authorized harvesting of hay during the 1988 crop year on croplands subject to a conservation reserve program contract, there shall be no reduction in the rental payments, which would otherwise occur as a result of the harvesting, to the extent that the producer pays for additional approved conservation practices. The amount of the avoided reduction is limited to one-half of the costs incurred for the new conservation measures. For example, assume that a producer entitled to rental payments of $100 x per year would normally be subject to a reduction of $25x in 1989 (and thus would receive only $75 x) if the producer harvested hay during 1988 pursuant to the emergency authorization. If the producer, however, pays at least $50x for additional approved conservation measures, the producer will receive the full

$100x in 1989.

In effect, the avoided-reduction portion of the rental payment is a cost-sharing payment for the additional conservation **[*14]** measures. This portion, however, is not excludible from gross income because it is not made pursuant to a program specified in section 126 of the Code. The balance of the rental payment is also not excludible from gross income under section 126. A producer, therefore, should include the full rental payment in gross income. The conservation costs that the producer pays or incurs may be recovered under the normal rules applicable to costs incurred for such conservation measures (*e.g.,* through current deduction, depreciation, amortization or upon disposition). See section 175, which permits a current deduction of soil or water conservation expenses if certain requirements are met.

PROCEDURAL INFORMATION

This notice serves as an "administrative pronouncement" as that term is described in section 1.6661-3 (b) (2) of the regulations and may be relied upon to the same extent as a revenue ruling or revenue procedure.