



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, DC 20224

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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--
SUPPLEMENTAL PAYMENTS FROM THE
STATE ACQUISITION AND RELOCATION FUND

This technical assistance request is in response to your request for assistance dated December 15, 1999, regarding the tax treatment of payments made to individuals and business in North Carolina that 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 State supplemental payments includible in the recipients' gross incomes if made to enable homeowners to purchase comparable housing outside the 100-year flood plain after their damaged homes in the flood plain were purchased under a federally assisted program?

CONCLUSION:

The State's supplemental payments to enable homeowners to purchase comparable housing outside the flood plain after their damaged homes in the flood plain were purchased under a federally assisted program are in the nature of general welfare and are not includible in the recipients' gross incomes. The State should not issue Forms 1099 for the payments because they are not includible in a recipient's income.

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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 extensive and prolonged flooding that devastated the civil, social, economic, and environmental well-being of eastern North Carolina. The entire economic base of that area 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 consisting of numerous relief programs to assist individuals and small businesses in recovering from this disaster. The "Hurricane Floyd Recovery Act of 1999" was enacted on December 16, 1999.

The following disaster assistance program is addressed in this Technical Assistance. The number appeared in the margin of materials in your request for assistance. We are providing our assistance regarding other State programs in other memoranda.

Supplemental Payments From the State Acquisition and Relocation Fund (1)

The federal government will purchase certain homes in flood-prone areas at the pre-flood fair market value. In many cases, homeowners are unable to purchase comparable housing outside the 100-year flood plain at that value. This grant program will provide supplemental payments to those homeowners, thereby enabling them to purchase comparable replacement homes. The average supplemental payment is expected to be \$25,000, but will vary depending on the cost differential between the pre-flood value of the home and the cost of a comparable home in a less flood-prone area.

Homeowners are eligible for a supplemental payment if they relocate in the same geographical area and occupy the replacement home for at least 5 years. If the replacement home is sold within 5 years, a prorated portion of the supplemental payment must be repaid to the State.

LAW AND ANALYSIS:

Section 61(a) of the Internal Revenue Code and the Income Tax Regulations thereunder provide that, except as otherwise provided by law, gross income means all income from whatever source derived.

However, the Service has held that payments made under legislatively provided social benefit programs for the promotion of general welfare are not includible in an

individual's gross income (the general welfare exception). See, e.g., Rev. Rul. 74-205 (replacement housing grants received by individuals under the Housing and Urban Development Act of 1968 are in the nature of general welfare and are not includible in their gross income) and Rev. Rul. 98-19, 1998-1 C.B. 840 (relocation payments authorized under the Housing and Community Development Act of 1974, made by a local jurisdiction to an individual moving from a flood-damaged residence to another residence, are not includible in an individual's gross income).

We will treat the State's program as making an outright payment to the recipient, and not a loan, because the recipient controls whether any repayment is required. Further, in comparing the State's supplemental payments to those in the Service's rulings, we find sufficient similarity to treat the State's payments under this program the same as the payments in the cited rulings.

Accordingly, we suggest that you advise the State of North Carolina that the supplemental payments are not includible in the recipients' gross incomes, and that information reporting is not required on such payments. Further, we suggest that you advise the State of North Carolina to describe the tax consequences of these grants to the recipients in language similar to the following:

The Internal Revenue Service has advised us that you need not include in income State supplemental payments that enable you to purchase comparable housing outside the 100-year flood plain after your flood-damaged home was purchased under a federally assisted program.

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 any questions about this memorandum, please call George Baker at (202) 622-4920.