

CROP MARKETING STRATEGIES

Deferring 2008 Crop Insurance Indemnity Payments

Crop insurance providers are reporting large loss payments this fall. The early losses were noted from production losses: prevented planting, replant, flooding and hail claims. In recent weeks, the decline in December corn futures and November soybean futures prices during October and November triggered large revenue loss claims. These losses are associated with revenue products such as Crop Revenue Coverage (CRC), Revenue Assurance (RA) and Group Risk Income Protection (GRIP). Of all the corn and soybean insurance policies sold in Iowa for 2008, approximately 80 percent of the acres were covered by these revenue products.

Both CRC and RA policies are farm-level products that guarantee revenue (yield times price) for corn and soybeans acres insured. The revenue guarantee determines the price using the average daily futures settlement prices in the month of February. For corn, the December corn futures contract is used and for soybeans, the November soybean futures contract. In February 2008, the spring base price was \$5.40/bu for corn and \$13.35/bu for soybeans, respectively. These prices are multiplied times the actual production history (APH) as reflected by a unit (optional, basic, whole farm or enterprise).

GRIP policies are county-level products. A county yield is reflected in determining coverage. Claims are then based annually on the final county yield determined by the USDA National Ag Statistics Service (NASS) and released in the late winter.

An insured with farm-level products such as CRC or RA could simply multiply their actual harvest yields times the fall price to determine the 'revenue to count.' This amount is then subtracted from their revenue guarantee. These CRC and RA policies guaranteed soybean growers the difference between the \$13.36/bu spring base price and the \$10.36/bu or \$9.22/bu harvest price. CRC plans capped the payout at \$3 per bushel difference in the spring base price, while RA had no cap. For CRC corn, harvest price was \$4.13/bu determined during the month of October using the daily settlement futures price for December corn. The RA harvest price was \$3.74/bu, since it was determined during the month of November.

Crop	CRC/GRIP Coverage	RA Coverage
Corn: Spring Base Price \$5.40/bu	Fall Price: \$4.13/bu Difference \$1.27/bu 23.5% decrease	Fall Price: \$3.74/bu Difference \$1.66/bu 30.7% decrease
Soybeans: Spring Base Price \$13.36/bu	Fall Price: \$10.36/bu Difference \$3.00/bu 22.5% decrease	Fall Price: \$9.22/bu Difference \$4.14/bu 31% decrease

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Tax Treatment for Revenue Losses

Tax practitioners report a widespread phenomenon this fall: farmers are receiving crop insurance claims without incurring a physical loss of yield from natural disasters. Such insurance claims do not arise from qualifying weather-related events to allow deferral of income to 2009 under IRC Sec. 451(d). However, if the loss is primarily due to a price decline and not a production loss, the income is taxable in the year received. For GRIP policies,

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indemnity payments will not be made until the USDA NASS determines final county yields. That information is anticipated to be released on March 2nd. So those payments will likely be 2009 taxable income.

Tax Treatment for Production Losses

The tax code only allows deferral of crop insurance claims to the next tax year when the insurance is received from production loss; a casualty or natural disaster such as a drought, hail, frost, wind, flood or prevented planting. It does not offer flexibility to shift income between tax years for victims of a price declines such as those that triggered most of the large revenue losses in 2008. So if an indemnity payment is received during 2008 and is reflected primarily by the drop in price, it is likely taxable that year.

For any crop insurance claim that is primarily a production loss, a second requirement allows crop insurance deferral only if the grower's normal practice is to report the income in the following tax year. A recent Tax Court case denied deferral for a grower on the grounds that his marketing contract committed only 35 percent of his sales in the next crop year (Nelson, 130 TC No. 5). The IRS and the Tax Court maintained that a grower must normally sell half of his crop the following year to qualify for the income tax deferral.

A third requirement is that each trade or business must defer all qualified payments if they choose the election, so an insured can't split their income. Thus the election is an "all-or-nothing" decision.

Conclusion

Crop insurance proceeds based on revenue protection and received in 2008 are not eligible for deferral to 2009. Farmers might want to provide along with their 2008 tax information copies of statements received from the insurance carrier identifying how the claim was determined. The type of crop insurance loss is important in determining the tax treatment for indemnity payments. Fortunately, the documentation by crop insurance carriers clearly differentiates the amounts that occurred from production and those from price declines.

Always seek advice from a certified tax preparer regarding crop insurance indemnity payments and how they are to be treated for tax purposes.

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