Disaster and Crop Insurance Payments

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Any crop insurance proceeds you receive need to be included as income on your tax return. You generally include that income in the year the payment is received. Crop insurance also includes crop disaster payments received from the federal government as a result of destruction or damage to crops, or the inability to plant crops, because of drought, flood, or any other natural disaster.

According to IRS Publication 225 (The Farmers Tax Guide -- http://www.irs.gov/pub/irs-pdf/p225.pdf) you can postpone reporting crop insurance proceeds as income until the year following the year the damage occurred if you meet all the following conditions:

a. You use the cash method of accounting.

b. You receive the crop insurance proceeds in the same year the crops are damaged.

c. You can show that under normal business practice you would have included income from the damaged crops in any tax year following the year the damage occurred.

Generally, farmers are able to establish their practice of reporting crop income in a following taxable year by reference to their prior year’s sale records. In order for a payment to constitute insurance for the destruction of or damage to crops, the insured must suffer actual physical loss. Agreements with the insurance companies that provide for payments without regard to actual losses by the insured, such as payments in the event that county average yield is less than a specified amount, are not payments for the destruction of or damage to crops. Such payments do not qualify for deferral under I.R.C. § (Internal Revenue Code Section) 451(d). Also payments made for a decline in the price of the commodity, rather than a physical loss, do not qualify for deferral.

An indemnity payment from a Revenue Protection (RP) policy is based on price as well as quantity and quality of the commodity produced. **Only the payment for destruction or damage (yield loss) is eligible for deferral.** A farmer who receives compensation from a RP policy must determine the portion of the payment that is due to crop destruction or damage rather than due to a reduced market price.

An insurance payment received from a prevented planting policy does qualify for crop insurance deferral (assuming the taxpayer meets all other requirements for deferral). This provision is addressed specifically in IRS code section 451(d).

A RP policy guarantees a minimum amount of revenue per acre for the insured farmer. The policy provides a formula for computing the deemed revenue the insured received from the crop that was produced. Taken into account is price of the commodity at the time of harvest, the quantity the insured farmer harvested and the quality of the commodity harvested. This deemed revenue is compared with the guaranteed minimum revenue. The excess of the guaranteed minimum over the deemed revenue received is the amount paid to the insured farmer.

**Note:** This information piece is offered as educational information only and is not intended to be tax, legal or financial advice. For questions specific to your farm business or individual situation, consult with your tax preparer.