Tax Treatment of Residential Grants Made by the Lower Manhattan Development Corporation to Individuals and Families Affected by the September 11, 2001, Disaster

Notice 2002–76

PURPOSE

This notice provides answers to frequently asked questions regarding the tax treatment of Residential Grant Program grants the Lower Manhattan Development Corporation (the LMDC) makes to individuals and families who occupy rental units or owner-occupied units in areas near the site of the September 11, 2001, attack on the World Trade Center.

BACKGROUND

Residential Grant Program

The LMDC, a subsidiary of the Empire State Development Corporation, which is a public benefit corporation of the State of New York, was created in the aftermath of the September 11, 2001, attack on the World Trade Center. In cooperation with city, state, and federal agencies, the LMDC developed the Residential Grant Program to offer financial assistance to individuals who reside, or will reside, in areas near the site of the World Trade Center disaster. The LMDC received its funding for the Residential Grant Program from the United States Department of Housing and Urban Development. The LMDC's Partial Action Plan, as amended on September 25, 2002, and implemented on September 26, 2002, describes the Residential Grant Program.

The Partial Action Plan divides the areas closest to the World Trade Center disaster site into three zones (Zone 1, Zone 2, and Zone 3). These three zones correspond generally to the locations of those residents who experienced the most exposure to the effects of the disaster.

The LMDC Residential Grant Program offers three types of grants to families and individuals residing in areas closest to the World Trade Center disaster. The first grant is a one-time $1,000 grant available only to residents who occupied a housing unit in Zone 1, 2, or 3 before September 11, 2001, and continue to live there through the date of their application and the date of the award.

The second grant is for families with one or more children under the age of 18 making a 1-year commitment to occupy rental units or owner-occupied housing in Zone 1, 2, or 3 ("family grants"). These grants are available regardless of whether the grant recipient resided in Zone 1, 2, or 3 on September 11, 2001. The one-time grant amount is $1,500 if the unit is in Zone 1 and $750 if the unit is in Zone 2 or 3. The Partial Action Plan states that the family grants are intended to compensate families for the extra expenses they incurred or will incur because of the continuing effects of the September 11, 2001, disaster. The family grants are expected to be reasonably commensurate with the extra reasonable and necessary personal, living, and family expenses that grant recipients have incurred or will incur as a result of the September 11, 2001, disaster, from the time they commenced residing in Zone 1, 2, or 3 through the first anniversary after the grant is made, excluding personal, living, or family expenses that are reimbursed from other sources, including the Federal Emergency Management Agency ("FEMA") and private insurance.

The third grant is for individuals making a 2-year commitment to occupy rental units or owner-occupied housing in Zone 1 or 2 ("2-year commitment grant program"). These grants are available regardless of whether the grant recipient resided in Zone 1 or 2 on September 11, 2001. In general, these grants equal 30 percent of monthly rent or, for owner-occupied units, 30 percent of mortgage payments, maintenance, and real estate and related taxes. The maximum grant amount is $12,000 over 2 years for Zone 1 units, and $6,000 over 2 years for Zone 2 units. The minimum grant amount is $4,000 over 2 years for units in Zone 1 and $2,000 over 2 years for units in Zone 2.

The Partial Action Plan states that the minimum grants ($4,000 per unit in Zone 1 and $2,000 per unit in Zone 2) are intended to compensate those residents who incurred or will incur extra expenses because of the continuing effects of the September 11, 2001, disaster. The minimum grant amounts are expected to be reasonably commensurate with the extra reasonable and necessary personal, living, or family expenses that grant recipients have incurred or will incur as a result of the September 11, 2001, disaster, from the time they commenced residing in Zone 1 or 2 through the second anniversary after the initial grant payment is made, excluding personal, living, or family expenses that are reimbursed from other sources, including FEMA and private insurance.

Overview of the General Welfare Exclusion and Information Reporting Requirements

Section 61(a) of the Internal Revenue Code provides that, except as otherwise provided by law, gross income means all income from whatever source derived. The Internal Revenue Service, however, has consistently held that payments by governmental units under legislatively provided social benefit programs for the promotion of the general welfare are not includible in a recipient's gross income (general welfare exclusion). *See e.g.*, Rev. Rul. 74–205, 1974–1 C.B. 20; Rev. Rul. 98–19, 1998–1 C.B. 840. To qualify under the administrative general welfare exclusion, the payments must (i) be made from a governmental fund, (ii) be for the promotion of general welfare (based on need), and (iii) not represent compensation for services. Rev. Rul. 75–246, 1975–1 C.B. 24; Rev. Rul. 82–106, 1982–1 C.B. 16.

Governmental payments to help individuals and families meet disaster-related expenses are based on need. For example, Rev. Rul. 76–144, 1976–1 C.B. 17, holds that grants made under the Disaster Relief Act of 1974 to help individuals or families affected by a disaster meet extraordinary disaster-related necessary expenses or serious needs in the categories of medical, dental, housing, personal property, transportation, or funeral expenses (and not in the categories of nonessential, decorative, or luxury items) are excluded from gross income under the general welfare exclusion. In this context, because "need" is not defined in terms of financial need, the general welfare exclusion applies equally to all residents of an affected area regardless of their income levels. In the absence of a disaster, however, governmental payments made without regard to financial status, health, educational background, or employment status are not based on need and, thus, do not qualify under the general welfare exclusion. *See* Rev. Rul. 76–131, 1976–1 C.B. 16; and Rev. Rul. 85–39, 1985–1 C.B. 21.

The Victims of Terrorism Tax Relief Act of 2001, Pub. L. No. 107–134, 115 Stat. 2427 (2001), added § 139 to the Code. Section 139(b)(4) codifies (but does not supplant) the administrative general welfare exclusion for certain disaster relief payments to individuals. Because "of the extraordinary circumstances surrounding a qualified disaster, it is anticipated that individuals will not be required to account for actual expenses in order to qualify for the [§ 139] exclusion, provided that the amount of the payments can be reasonably expected to be commensurate with the expenses incurred." Joint Committee on Taxation Staff, *Technical Explanation of the "Victims of Terrorism Tax Relief Act of 2001," as Passed by the House and Senate on December 20, 2001*, 107th Cong., 1st Sess. (2001). As under § 139, the Service will not require individuals to account for actual disaster-related expenses for governmental payments to qualify under the administrative general welfare exclusion if the amount of the payments can be reasonably expected to be commensurate with the expenses incurred.

Under § 6041 and the regulations thereunder, any person (including an agency of a state or its political subdivisions) engaged in a trade or business and making payments in the course of such trade or business to another person of fixed or determinable gains, profits, or income of $600 or more during a calendar year must provide an information return setting forth the amount of such gains, profits, and income, and the name and address of the recipient of the payment.

QUESTIONS AND ANSWERS

Q–1. *Are the one-time $1,000 grants excluded from gross income?*

A–1. Yes. The one-time $1,000 grants are excluded from grant recipients' gross income under the general welfare exclusion. These grants are intended to compensate individuals for the extra reasonable and necessary personal, living, and family expenses they incur as a result of the effects of residing in the area of the World Trade Center disaster and are expected to be commensurate with the expenses incurred. The $1,000 one-time grants also qualify for exclusion from gross income under § 139.

Q–2. *Are the family grants and the minimum grants under the 2-year commitment grant program excluded from gross income?*

A–2. Yes. The family grants ($1,500 for units in Zone 1 and $750 for units in Zone 2 or 3) and the minimum grant amounts ($4,000 for units in Zone 1 and $2,000 for units in Zone 2) under the 2-year commitment grant program are excluded from gross income under the general welfare exclusion. These grants qualify under the general welfare exclusion because these grants are intended to compensate individuals for unreimbursed extra reasonable and necessary personal, living, and family expenses they incur as a result of the continuing effects of the World Trade Center disaster and are expected to be commensurate with the expenses incurred. The family grants and the minimum grant amounts also qualify for exclusion from gross income under § 139.

Q–3. *Are the payments in excess of the minimum grant amounts under the 2-year commitment grant program excluded from gross income?*

A–3. No. The payments in excess of $4,000 for Zone 1 units and in excess of $2,000 for Zone 2 units under the 2-year commitment grant program do not qualify for exclusion from gross income under the general welfare exclusion or any other provision of law. These payments are distinguishable from the other grant payments under the Residential Grant Program because these payments are not intended to compensate individuals for the extra reasonable and necessary personal, living, and family expenses they incur as a result of residing in the area of the World Trade Center disaster. In addition, these payments are made regardless of any other needs-based criterion (for example, financial status, health, educational background, or employment status of the individual recipient). Grant recipients must include the remaining grant amounts under the 2-year commitment grant program in gross income under § 61(a).

Q–4. *Must grant recipients maintain records of the extra personal, living, and family disaster-related expenses they incurred to exclude from gross income under the general welfare exclusion payments of the one-time $1,000 grants, the family grants, and the minimum grant amounts under the 2-year commitment grant program?*

A–4. No. Grant recipients are not required to maintain records of the extra personal, living, and family disaster-related expenses they incurred to exclude from gross income under the general welfare exclusion payments of the one-time $1,000 grants, the family grants, and the minimum grant amounts under the 2-year commitment grant program.

Q–5. *Are payments of the one-time $1,000 grants, the family grants, and the minimum grants under the 2-year commitment grant program subject to information reporting by the LMDC?*

A–5. No. Payments of the following grants:

(1) the one-time $1,000 grants;

(2) the family grants ($1,500 for units in Zone 1 and $750 for units in Zone 2 or 3); and

(3) the minimum grant amounts under the 2-year commitment grant program ($4,000 for units in Zone 1 and $2,000 for units in Zone 2) are not subject to information reporting because these payments are excluded from gross income under the general welfare exclusion.

Q–6. *Are the payments in excess of the minimum grant amounts under the 2-year commitment grant program subject to information reporting?*

A–6. Yes. Because payments in excess of the minimum grant amounts under the 2-year commitment grant program must be included in gross income, LMDC must file with the Service and furnish to a grant recipient a Form 1099–G, *Certain Government Payments*, if the grant recipient receives $600 or more of such payments during a calendar year.

DRAFTING INFORMATION

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