

**INTERNAL REVENUE SERVICE**  
**NATIONAL OFFICE TECHNICAL ADVICE MEMORANDUM**

October 23, 2001

Number: **200211005**  
Release Date: 3/15/2002  
Index (UIL) No.: 3121.02-00  
CASE MIS No.: TAM-119114-01/TEGE:EOEG:ET1

Area Director  
Appeals SB/SE - Area 1

Taxpayer's Name:  
Taxpayer's Address:

Taxpayer's Identification No:  
Years Involved:  
Date of Conference:

**LEGEND:**

Taxpayer X =

Taxpayer Y =

Boat 1 =

Boat 2 =

Year 1 =

Year 2 =

**ISSUES:**

1. Whether in Year 1, Taxpayer X's services as a crew member of Boat 1 constituted service described in section 3121(b)(20) of the Internal Revenue Code (Code).
2. Whether in Year 2, Taxpayer X's services as a crew member of either Boat 1 or Boat 2 constituted service described in section 3121(b)(20) of the Code.

**FACTS:**

Taxpayer X and Taxpayer Y are spouses. Taxpayer X works as a commercial

TAM-119114-01

fisherman. In Year 1, he worked as a crew member aboard Boat 1 and frequently was the captain of the vessel. Taxpayer X worked on 49 trips during Year 1. There were never more than four crew members on Boat 1 on any trip. Under an arrangement with the owner of Boat 1, Taxpayer X received a share of the proceeds from the sale of the fish caught from each trip. The owner deducted trip expenses from the gross proceeds. The balance was then split with a certain percentage of the proceeds kept by the owner and the remaining portion of the proceeds paid to the crew members. For each trip, the amount of the catch and expenses are listed on the settlement sheets. In addition to net proceeds from the sale of the fish caught from each trip, the owner paid additional amounts to Taxpayer X in Year 1 to fund health insurance premiums.

For approximately the first six weeks of year 2, Taxpayer X continued to work on Boat 1. Taxpayer X continued to be paid in the same manner, except that Boat 1's owner did not pay any additional amounts towards health insurance premiums. At some point in February of Year 2, Taxpayer X began to work on another fishing vessel, Boat 2. There were never more than four crew members per trip on Boat 2. As a crew member, Taxpayer X received for each trip a percentage of the net proceeds from the sale of the catch. The owner of Boat 2 did not pay any other additional amounts to Taxpayer X in Year 2.

The owners of both Boat 1 and Boat 2 issued Forms 1099 reporting the net proceeds received by Taxpayer X. Taxpayers X and Y reported these amounts on Schedule C of their Forms 1040. Taxpayers X and Y did not report any self-employment income or pay any Self-Employment Contributions Act (SECA) tax on their Year 1 and Year 2 returns.

## **LAW AND ANALYSIS**

Under section 3121(b)(20) of the Internal Revenue Code (Code), services performed by an individual on a fishing boat are not included as employment for purposes of the Federal Insurance Contributions Act (FICA) tax if performed under an arrangement with the owner or operator of the boat under which (1) the individual receives only a share of the boat's catch or the proceeds from such catch, (2) the amount of the individual's share depends on the amount of the boat's catch, and (3) the individual receives no other cash remuneration beyond remuneration that does not exceed \$100 per trip, is contingent on a minimum catch, and is paid solely for additional duties for which additional cash remuneration is traditional in the industry. In addition, the operating crew of the boat must normally be made up of fewer than 10 individuals, which means that the average size of the operating crew on trips made during the preceding four calendar quarters consisted of fewer than 10 individuals.

Revenue Ruling 77-102, 1977-1 C.B. 300, addresses two situations as to whether the services performed by certain individuals are excepted from "employment" under section 3121(b)(20). In Situation 1, the owner of a fishing boat employs a captain and

TAM-119114-01

eight other crew members to perform services on the boat, which is engaged in catching fish. The crew members receive payments of the net proceeds of the boat's catch, computed as follows:

1. out of the gross proceeds from the sale of the catch deductions are made for certain specified expenses such as ice, fuel, and a payment of \$25 each to the mate, engineer, and cook;
2. 60 percent of the remaining proceeds (net stock) is divided equally among the captain and other crew members, and the remaining 40 percent is divided between the captain and the owner.

Before each trip, the crew members are responsible for loading supplies and doing other necessary work in port in preparation for the trip. At the completion of the trip, the crew must remove and transport the catch to the point of sale and perform other incidental duties necessary to leave the boat in the same condition as it was before the trip. These duties, which may include repairing nets, constructing new nets, and splicing cable, are performed without additional remuneration.

The ruling holds that because the \$25 payments do not depend upon the amount of the boat's catch, the arrangement with the mate, engineer and cook fails to meet the requirements of section 3121(b)(20). The ruling further holds that the services performed by the other six crew members are excepted from employment because they do not receive any cash remuneration other than a share of the proceeds from the sale of the catch. Their share depends on the amount of the catch.

In Situation 2, the facts are the same, except the arrangement also provides that for each trip the captain and other crew members, in addition to receiving a share of the catch, are entitled to receive X dollars per hour for repairing nets, constructing new nets, splicing cable, and doing other incidental work while in port. In Situation 2, all of the crew members are entitled to receive cash remuneration other than a share of the catch. The ruling holds that none of their services are excepted from employment under section 3121(b)(20).

Treas. Reg. § 31.3121(b)(20)-1(a)(1)(ii), which was promulgated in 1980, provides that an individual's service on a boat engaged in catching fish is excepted from employment only if the amount of the individual's share depends solely on the amount of the boat's catch of fish. Section 31.3121(b)(20)-1(a)(2) explains that this requirement is not satisfied if there exists an agreement with the boat's owner or operator by which the individual's remuneration is determined partially or fully by a factor not dependent on the size of the catch. For example, if a boat is operated under a remuneration agreement, e.g., a collective agreement which specifies that crew members, in addition to receiving a share of the catch, are entitled to an hourly wage for repairing nets, regardless of whether this wage is actually paid, then all the crew members covered by

TAM-119114-01

the arrangement are entitled to receive cash remuneration other than a share of the catch and their services are not excepted from employment by section 3121(b)(20).

Taxpayers argue, however, that the language of § 31.3121(b)(20)-1 conflicts with the holding in Rev. Rul. 77-102. Section 31.3121(b)(20)-1 provides that in order to qualify for the exception under section 3121(b)(20), the remuneration of the crew member must be determined solely based on the catch. The taxpayers believe that a payment of a percentage of the catch after deduction for expenses is not based solely on the catch, because the expenses deducted may not relate to the size of the catch. The example provided in the regulation, however, clarifies that the requirement that the payment be based solely on the catch requires that the compensation be calculated by reference to the catch, in contrast to a set fee or hourly wage arrangement.

Taxpayers argue that Rev. Rul. 77-102 is an incorrect application of section 3121(b)(20), and is inconsistent with the relevant regulations. The same argument concerning the validity of Rev. Rul. 77-102 was raised by the taxpayers in Flamingo Fishing Corp. v. United States, 32 Fed. Cl. 377, 380 (1994). The court held that the interpretation of the statute in Rev. Rul. 77-102 represented a reasonable position and therefore was valid. The court also upheld the validity of Treas. Reg. § 31.3121(b)(20), and found no inconsistency between the regulations and Rev. Rul. 77-102. Therefore, the principles set forth in the regulations and Rev. Rul. 77-102 continue to be the applicable principles for determining whether a fisherman's services on a commercial fishing boat constitute service described in section 3121(b)(20) of the Code.

The additional amounts that the owner of Boat 1 paid to Taxpayer X in Year 1 to fund health insurance premiums constitute compensation for services rendered on the boat that is not a share of the boat's catch, does not depend on the amount of the boat's catch, and is not paid solely for additional duties for which additional cash remuneration is traditional in the industry. Therefore, Taxpayer X's services did not qualify for the section 3121(b)(20) exception from employment in Year 1. Because Taxpayer X did not receive any additional payments for Year 2, either from the owner of Boat 1 or the owner of Boat 2, Taxpayer X's services did qualify for the section 3121(b)(20) exception from employment in Year 2.

#### **CONCLUSIONS:**

1. In Year 1, Taxpayer X's services as a crew member of Boat 1 did not constitute service described in section 3121(b)(20) of the Code.
2. In Year 2, Taxpayer X's services as a crew member of both Boat 1 and Boat 2 constituted service described in section 3121(b)(20) of the Code.

#### **CAVEATS:**

TAM-119114-01

A copy of this technical advice memorandum is to be given to the taxpayers. In accordance with section 6110(k)(3) of the code, this memorandum should not be cited as precedent.