



Income Tax Management for Ag Producers

Jason Grunewald, CPA

Senior Tax Specialist, Agcountry Farm Credit Services

Agenda



- Forced Livestock Sales
- Deferred Crop Sales
- Crop Insurance and Disaster Payments
- Net Operating Losses
- Like-Kind Exchanges
- Depreciation

Forced Livestock Sales



- **Section 451(g) deferral**

- Gain on Weather related sales of any livestock may be deferred for 1 year
 - May defer reporting income from livestock sold because of drought, flood, or other-related conditions
 - Designation can be made by the President, Department of Ag, or other federal departments to declare a disaster area.
- Deferrable gain is calculated based upon the difference of the quantity sold due to adverse weather conditions compared to the quantity sold during normal business practices.

Forced Livestock Sales



- **Section 451(g) deferral - Example**

- Your County has been declared a disaster area due to Drought
- You typically sell 50 cows from your beef herd each year.
- This year due to reduced grassland and access to feed you sell 75 cows

- You can defer the sale of 25 cows until 2022 under Section 451(g)

Forced Livestock Sales



- **Section 1033(e) involuntary conversions**

- Sales of livestock held for draft, dairy or breeding purposes
 - Sales exceed the number that would normally be sold during the normal time period
 - Sales occur because of drought, flood, or other weather-related condition
 - No requirement for a federal disaster area
- Replacements
 - Must be purchased within 2 years
 - Must be replaced with similar (heifers for heifers) or related in service or use
 - Must be held for the same purpose that the animals given up were held
- In areas eligible for federal assistance, the 2-year period is extended to 4 years.

Forced Livestock Sales



- **Section 1033(e) involuntary conversions - Example**

- This year because of a drought you had to sell 80 heifers
- Normal sales of heifers for the past 3 years is 50 heifers
- Can postpone gain of 30 heifers until replacement heifers are purchased

- Replacements

- If replacements cost is less than gain, then amended return will need to be completed on prior return where gain was deferred
- If replacements are never purchased, then prior return will need to be amended to recognize total deferred gain plus interest

Forced Livestock Sales



- **Statement on Tax return in year the gain was realized**
 - Evidence of the weather-related conditions that forced the sale or exchange of the livestock.
 - The gain realized on the sale or exchange.
 - The number and kind of livestock sold or exchanged.
 - The number of livestock of each kind you would have sold or exchanged under your usual business practice.

Forced Livestock Sales



- **Statement on Tax return in year Replacement is Made**
 - The dates you bought the replacement property.
 - The cost of the replacement property.
 - Description of the replacement property (for example, the number and kind of the replacement livestock).

Deferred Payment Contracts



- **Constructive Receipt**

- Income is constructively received when an amount is credited to taxpayer's account or made available without restrictions.
- Funds are Constructively received when:
 - Deposited into taxpayer's account
 - Checks are created and held at Elevator or livestock barn
 - Funds are available to be drawn upon
 - Receiving a check in the mail, but depositing later



Deferred Payment Contracts

- **Installment Sale Treatment**

- Contract needs to be created and signed by the seller
- Funds cannot be received until specific date on contract
- Contract must be in writing
- Contract may provide for interest

- Contracts work best in smaller intervals on a contract-by-contract basis
 - 2,500 - 5,000 - or 7,500 bushel contracts OR
 - \$20,000, \$30,000, or \$50,000 intervals

- Work with accountant at tax time to determine if Contract should claim as income in year prior or left in year deposited.

Crop Insurance / Disaster Payment Deferral

- **Insurance Deferral Requirement**

- Insurance payments received as a result of destruction or damage to crops
 - Floods, hail, wind, drought, etc.
- Under normal business practice the income would have occurred in a tax year following the year of destruction
 - Over 50% of crop traditionally sold in year following harvest
- All eligible crop insurance must be deferred if election to defer is chosen on tax return.
 - Revenue protection insurance typically does not qualify for insurance deferral.

Crop Insurance / Disaster Payment Deferral

- **Disaster Payments**

- Disaster payments received as a result of destruction or damage to crops
 - Floods, hail, wind, drought, etc.
- Can be deferred along with crop insurance.
 - Cannot choose to defer just one
- Typically, disaster payments are paid the year after harvest, which does not allow for deferral.



Net Operating Losses

- Net Operating losses occur when a business or individual has more allowable deductions than adjusted gross income
 - Before TCJA
 - 5-Year or 2-year carryback or elect to carryforward 20 years
 - After TCJA (2018-2020)
 - No carryback for business' other than farmers
 - Farmers retained a 2-year carryback
 - \$500,000 carryback limit and can only offset 80% of taxable income



Net Operating Losses

- CARES Act (Passed March 27, 2020)
 - Allows all business' a 5-year carryback for losses in 2018, 2019, or 2020.
 - Delays 80% of taxable income limit
 - Amended return can be filed for 2018, or 2019
 - Farmers also retained a 2-year Carryback
- 2021 forward
 - No carryback for other business'
 - Farmers retained a 2-year carryback
 - \$500,000 carryback limit and can only offset 80% of taxable income

Like-Kind Exchange (1031)



- **History**

- Before TCJA
 - Like-Kind exchanges (LKE) were allowed for personal property and real property
 - Personal property includes farm machinery and vehicles
 - Real Property is rental property, land and buildings.
- Post TCJA
 - Eliminated LKE treatment of personal property
 - Trade of equipment a sale is recognized for the trade-in value
 - New asset is placed on the books at full list price

Like-Kind Exchange (1031)



- **Example #1**

- Farmers Trades in his combine.
- New Combine List price: \$500,000
- Trade-in value of old combine: \$350,000
- To Boot price: \$150,000

- Pre TCJA
 - New Combine listed as \$150,000 on Depreciation schedule
 - Old Combine is attached with the new combine
 - New combine is depreciated over 7 years or utilize S179 or bonus

Like-Kind Exchange (1031)



- **Example #1**

- Farmers Trades in his combine.
- New Combine List price: \$500,000
- Trade-in value of old combine: \$350,000
- To Boot price: \$150,000

- Post TCJA
 - New Combine listed as \$500,000 on Depreciation schedule
 - Old Combine is listed as a sale on form 4797 for \$350,000
 - Typically, S179 is utilized to offset the sale of 350,000

Like-Kind Exchange (1031)



• **Potential Issues**

- No self – employment tax due to Sch F offsetting form 4797
- Some states do not conform to S179 or Bonus depreciation limits
 - ND does conform to S179 and Bonus
 - MN conforms to S179 as of 2020, does not conform to Bonus rules
- North Dakota Property Exemption does allow form 4797 of farm equipment to qualify as farm income. New for 2021



Like-Kind Exchange (1031)

- **Real Property Exchanges**

- Agricultural Land
- Residential Real Estate
- Commercial Real Estate
- Land With depreciable structures may be traded, but could trigger gain

- Does not include
 - Stock (Public or closely held)
 - Partnership Interest
 - License or permit to operate a business on the land
 - Securities or evidence of indebtedness



Like-Kind Exchange (1031)

- **Personal Home/ Farmstead**

- Sell home and agricultural land separately
- Home portion can qualify for Section 121 personal home exclusion
 - Allows for up to \$500,000 MFJ or \$250,000 single filer of tax-free gain
- The agricultural portion may use the like-kind exchange deferral

- **Vacation Home**

- Does not qualify for 1031 by itself
- Must be converted to eligible property
- Personal use must be limited or eliminated
 - Safe harbor is available

Like-Kind Exchange (1031)



- **Requirements**

- Exchange of property rather than a sale
- Properties exchanged must be like-kind real estate
- Properties exchanged must both be held for productive use in a trade or for investment
- Exchange of properties must be simultaneous OR
 - Replacement property identified within 45 days AND
 - Replacement property sale has completed within 180 days of the identification or the due date of the return (including extensions), if shorter.

Like-Kind Exchange (1031)



- **Requirements**

- Exchange of property rather than a sale
- Properties exchanged must be like-kind real estate
- Properties exchanged must both be held for productive use in a trade or for investment
- Exchange of properties must be simultaneous OR
 - Replacement property identified within 45 days AND
 - Replacement property sale has completed within 180 days of the identification or the due date of the return (including extensions), if shorter.



Depreciation

- **Placed in Service**

- Asset is in a state of readiness for use in the taxpayer's trade or business
 - Asset does not have to be in use
 - Cannot be on order or sitting at the dealership
- Buildings
 - Placed in service on the date the building is substantially complete or in the state of readiness and availability

- **Section 179**

- Limit of \$1,050,000, reduced if total purchases over \$2,620,000
- Equipment must be above 50% business use or Section 179 must be recaptured



Depreciation

- **Bonus Depreciation – IRC Section 168(k)**

- Provides 100% deduction on each class of assets
 - New or Used Assets
 - Buildings Qualify for Bonus depreciation
 - No recapture on assets below 50% business use
- Scheduled to phase out if Congress does nothing

Year	%
2021	100%
2022	100%
2023	80%
2024	60%
2025	40%
2026	20%



QUESTIONS?

Income Tax Management for Ag Producers
Presented by: Jason Grunewald, CPA
Jason.Grunewald@agcountry.com
701-642-7607

