# Farm Tax Update
# Risk and Profit Conference

August 19, 2021

Mark Dikeman – KFMA Assoc Director
Clay Simons – KFMA SC Economist

# American Rescue Plan

## Paid Sick & Family Leave Credits

- Through Dec 31, 2020, FFCRA required certain employers to provide paid sick leave (up to 2 weeks) or paid family leave (up to additional 10 weeks) when employees impacted by COVID
- Credit to employer against payroll taxes
  - Either 100% or 66.67% of pay for sick leave, depending on the reason for leave
  - 66.67% of paid family leave
- Similar credit available for SE individuals

## Paid Sick & Family Leave Credits

- ARP extends employer payroll credit through 9/30/21
- Increases max wages per employee to $12,000 (was $10,000)
- Allows second round of paid sick leave from 4/1/21 to 9/30/21 (if sick leave taken in 2020)
- SE individuals can claim credits for leave taken between 1/1/21 and 9/30/21 on 2021 tax return
  - 60 days of family leave
  - 10 days of sick leave
- SE individuals can use 2020 SE earnings if results in a higher credit

# Employee Retention Credit

- ARP extends ERC through December 31, 2021
  - Was through June 30, 2021
  - Infrastructure and Jobs Act of 2021 eliminates credit in the 4th quarter
- 2021 ERC
  - Requires a 20% reduction in gross receipts in a calendar quarter compared to the same quarter in 2019
  - 70% credit on up to $10,000 wages per employee per qualifying quarter
  - $28,000 max credit per employee
  - Credit against employer share of SS and Medicare in Q1 and Q2
  - Credit against employer share of Medicare in Q3 and Q4
  - Reduce payroll deposits by credit amount, claim on 2021 Form 943, or request a refund with Form 7200

# Tax Planning Tools

## Tax Planning Strategies

- Minimize income tax (farmer/accountant philosophy)
  - Prepay expenses, maximize depreciation, hold grain inventory
  - Not always the best strategy
- Optimize after tax income (economist philosophy)
  - Look at the past, present, and future
  - Fully utilize standard deduction
  - Maximize marginal brackets

## Tax Planning Strategies

- Farmers have a host of tools available to manage tax liability
  - Increase expense
  - Decrease expense
  - Increase income
  - Decrease income
  - Income averaging
  - Maximizing credits

## Tax Planning Strategies

- Rules of thumb
  - Inventory change and taxable income change should usually be moving in the same direction
  - Taking §179 or bonus on financed equipment is deducting an expense that hasn't been paid for
  - In the long run, net farm income plus non-farm income should be greater than
    - Family living expense plus tax liability
    - Land principal payments

## Constructive Receipt

- Constructive receipt is the point where the you have control of funds
  - You have control of funds if you have received a check even if not deposited in the bank
  - You have control of funds if you have the ability to receive a check even if you have not received it

## Deferred Payment Contract

- Sale of grain or livestock with a contract for payment sometime in the future, usually the following tax year
- Must be a written contract between buyer (elevator or other firm that takes actual title) and seller (producer)
  - Is a sale barn the purchaser or an intermediary?
  - Specifies quantity, price, grade and timing of payment
  - No constructive receipt = seller has no right to the proceeds until the date specified in the contract (or there are substantial limitations or restrictions)

## Tax Planning Tools – ↑ Expense

- Accelerate depreciation (§179 or bonus)
  - Leave yourself some wiggle room if possible
- Prepay expenses
  - No more than 50% of total expense
  - Must be a business purpose (not just tax avoidance)
  - Must be actual purchase (not just down payment)
    - Specific quantity (gal, tons, lbs, etc)
  - Cannot deduct prepaid rent, insurance, or interest
- Maximize retirement plan contributions
- Large year-end charitable contributions

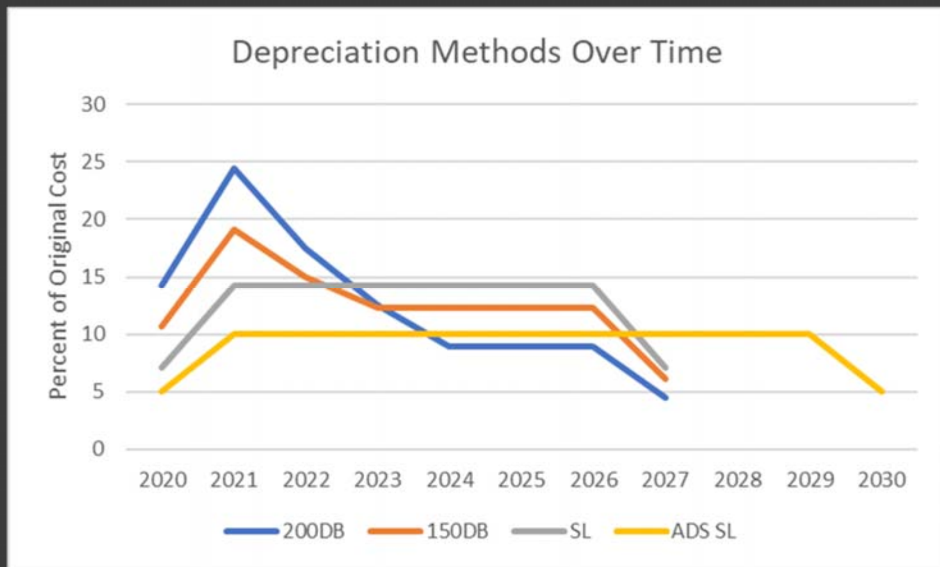
## Tax Planning Tools – ↑ Expense

- Maximize retirement plan contributions
- Charitable contributions

## Tax Planning Tools – ↓ Expense

- Slow down depreciation
  - Default farm depreciation is MACRS 200DB
  - Elect to use MACRS 150DB
  - Elect to use straight-line (SL)
  - Elect to use SL and use Alternative Depreciation System (ADS)
    - ADS increases depreciable life (usually)
- Capitalize long life repairs
  - Depreciate rather than deduct as a repair
  - Engine or transmission rebuild
- Capitalize long life fertilizer expense

# Tax Planning Tools – ↓ Expense




# Tax Planning Tools – ↑ Income

- Sell inventory
  - If grain is stored at home, it may not be possible to deliver & sell by year end
  - Grain may be contracted for delivery next year
  - Producer may not like the current price
- Sell/trade-in appreciated or low basis assets
- CCC loan on grain
  - Wheat = $3.38/bu, corn & milo = $2.20/bu, SB = $6.20/bu
  - Timeliness may be an issue for farm stored grain
  - Paperwork needed may deter some
  - Can create some accounting challenges when grain is sold

## Tax Planning Tools – ↑ Income

- Elect out of installment treatment on deferred payment contracts
  - Recognize income in the year of sale even when payment has not been received
  - Effective tax planning tool if there is uncertainty
  - Election is all or none on a contract-by-contract basis
    - Sell with multiple contracts in varying amounts
- Traditional to Roth IRA conversion
- Deemed dividend from S-Corporation
  - Only applies to S-corps with E&P (operated as a C-corp)

## Tax Planning Tools – ↓ Income

- Defer crop insurance
  - Available if proceeds received in year of production
  - Available if you normally sell > 50% of grain the following year
  - Only payments received for crop damage can be deferred
    - Revenue portion of crop insurance cannot be deferred
    - Weather insurance proceeds (based on rainfall) cannot be deferred
- Defer disaster payments
  - Usually not possible
  - CFAP payments were for price decline (not crop damage)
  - WHIP+ payments were for 2018 and 2019 production losses

## Tax Planning Tools – ↓ Income

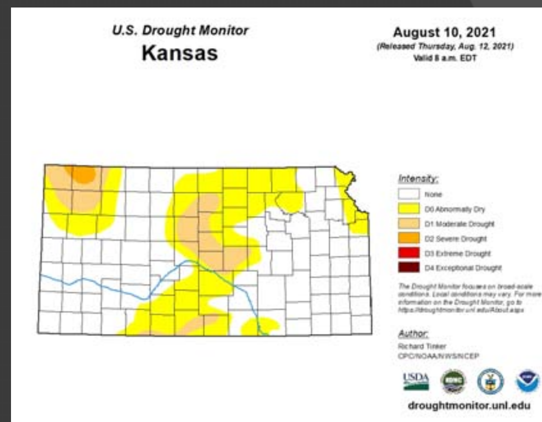
- Deferring crop insurance
  - You need the summary of loss to estimate revenue loss
    - Or have them call their crop insurance agent
  - Yield policies will not have a revenue loss component
  - Revenue policies *may* have a revenue component
  - Several methods to calculate revenue portion
    - Roger McEowen https://farmdocdaily.illinois.edu/2012/07/the-2012-drought-and-income-ta.html
    - RCIS calculates differently and reports revenue portion on their summary of loss (or used to)

## Tax Planning Tools – ↓ Income

- Defer drought related cattle sales
- Elect to defer taxation of sales in excess of normal sales
  - Cows or calves
    - Requires federal disaster declaration
    - Defer to the following tax year
  - Cows
    - Does not require disaster declaration, but be prepared to provide proof of weather issues
    - Defer until replacement is purchased or 2 years later (4 years if in a declared disaster area)
    - Decrease basis of replacement stock by amount deferred

# Tax Planning Tools – ↓ Income

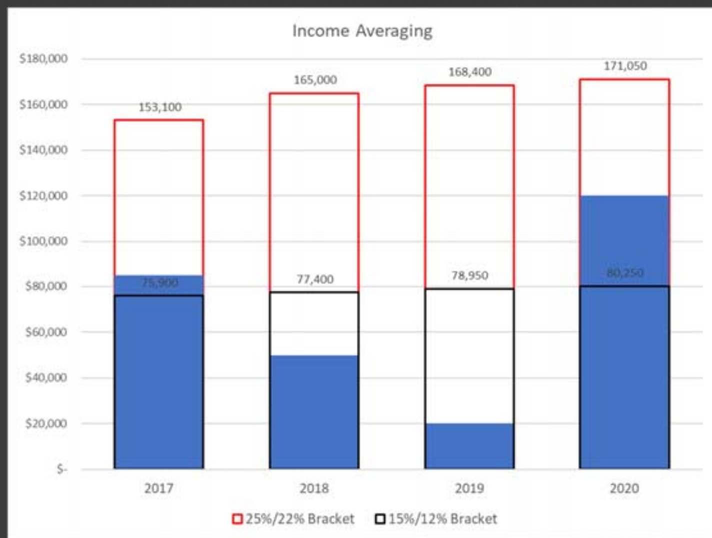
- Defer drought related cattle sales
  http://ruraltax.org/files-ou/Livestock_Sales.pdf
- 8/10/21 Drought Monitor Map



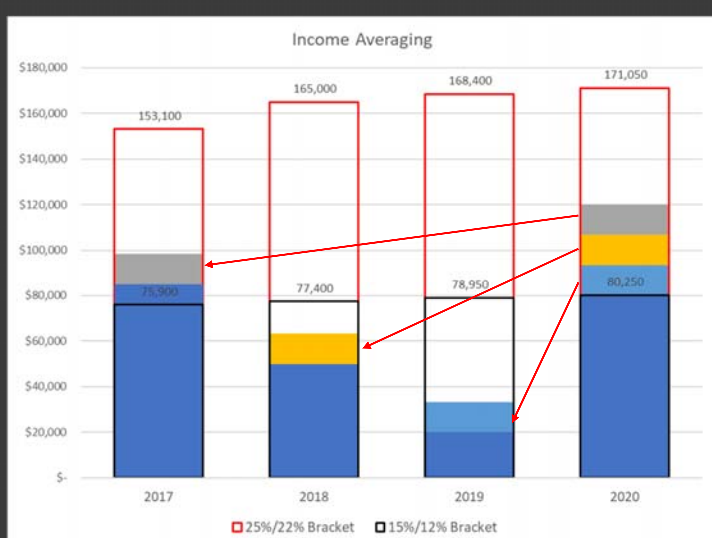

# Tax Planning Tools – Income Averaging

- Reported on Schedule J
- Elected farm income (amount averaged) spread over the three prior years; tax is recalculated & compared
- Can elect to average any amount up to Schedule F + 4797 gain
  - Gain from land sales is not eligible!!
  - Pass-through farm income is eligible as well
- Utilizes brackets in previous years that were not filled
- Does not affect SE tax
- Capital gain income in the current year (or prior years) complicates calculation and confuses the IRS

# Tax Planning Tools – Income Averaging




# Tax Planning Tools – Income Averaging



# Questions and Discussion