Agricultural and Natural Resources Issues

Chris Bruynis, David Marrison, and Barry Ward
How Has 2019 Been for our Ag Industry?

1. Historical Weather Issues in Eastern Corn Belt
2. Crop Insurance Payments Up in 2019 (see above)
3. Farm Bill Payments Lower in 2019 (or zero)
4. Trade War Continues with China - (soybeans)
5. Market Facilitation Program Payments (again)
6. Farm Economy is Still VERY Tight.
2018 Planting Season
June 15, 2018

2019 Planting Season: Frustrating

2019 Planting Season
June 15, 2019

Image Source: Wall Street Journal
Net farm income and net cash farm income, 2000-19F

$ billion (2019)

2000-18 average NFI

2000-18 average NCFI

Net cash farm income (NCFI)

Net farm income (NFI)

Note: F = forecast. Values are adjusted for inflation using the chain-type GDP deflator, 2019=100.
Data as of August 30, 2019.
Ohio Corn - Returns to Land

<table>
<thead>
<tr>
<th>Year</th>
<th>Returns to Land ($/Acre)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2005</td>
<td>46</td>
</tr>
<tr>
<td>2006</td>
<td>184</td>
</tr>
<tr>
<td>2007</td>
<td>336</td>
</tr>
<tr>
<td>2008</td>
<td>158</td>
</tr>
<tr>
<td>2009</td>
<td>79</td>
</tr>
<tr>
<td>2010</td>
<td>421</td>
</tr>
<tr>
<td>2011</td>
<td>549</td>
</tr>
<tr>
<td>2012</td>
<td>366</td>
</tr>
<tr>
<td>2013</td>
<td>148</td>
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<tr>
<td>2014</td>
<td>47</td>
</tr>
<tr>
<td>2015</td>
<td>47</td>
</tr>
<tr>
<td>2016</td>
<td>41</td>
</tr>
<tr>
<td>2017</td>
<td>78</td>
</tr>
<tr>
<td>2018</td>
<td>84</td>
</tr>
</tbody>
</table>
MAJOR STRESS FOR FARMERS!
Topics

Issue 1: Qualified Conservation Contributions
Issue 2: 2018 Farm Bill
Issue 3: Oil and Gas Interests
Issue 4: Income Tax Planning for Farmers
Issue 5: C Corp. Conversion to S Corp.
Issue 6: Getting out of the Business of Farming
Issue 7: Qualified Business Income Deduction for Cooperatives
Presentation Topic Order

Issue 2: 2018 Farm Bill
Issue 4: Income Tax Planning for Farmers
Issue 7: Qualified Business Income Deduction for Cooperatives
Issue 6: Getting out of the Business of Farming
Issue 1: Qualified Conservation Contributions
Issue 3: Oil and Gas Interests
Issue 5: C Corp. Conversion to S Corp.
Issue 2: 2018 Farm Bill

- Signed December 20, 2018
- Includes commodity, food, & nutrition, and crop insurance provisions
- Remains in place through 2023

Projected Costs of 2018 Farm Bill (FY 2019-2028)

- Commodities: 9%
- Conservation: 0.5%
- Nutrition: 7%
- Crop Insurance: 7%
- All Other: 77%
Dairy Margin Program

- The 2014 Margin Protection Program (MPP) was retooled to become the Dairy Margin Program (DCM).
- Annual or life of farm bill decision
- Annual fee to participate
- 2019 will generate taxable income – look for this with your dairy farmers.
Commodity Programs

- Ag Risk Coverage (ARC) and Price Loss Coverage (PLC) are continued with some modifications.
- PLC protects for low prices and ARC protects for low revenue.
2018 Farm Bill: Decisions to be Made

Elect a Federal Commodity Program

Agricultural Risk Coverage - County
Paid on 85% of Base Acres

Agricultural Risk Coverage - Individual
Paid on 65% of Base Acres

Price Loss Coverage
Paid on 85% of Base Acres

Supplemental Coverage Option
Paid on COMBO Purchased Planted Acres

<table>
<thead>
<tr>
<th>Share of Base Acres Enrolled in PLC 2018</th>
<th>Nationally</th>
<th>Ohio</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corn</td>
<td>7%</td>
<td>2%</td>
</tr>
<tr>
<td>Soybeans</td>
<td>3%</td>
<td>2%</td>
</tr>
<tr>
<td>Wheat</td>
<td>42%</td>
<td>18%</td>
</tr>
</tbody>
</table>

Data Source: USDA-FSA, ARC and PLC Landing Page
# ARC and PLC Payments (State Average)

<table>
<thead>
<tr>
<th></th>
<th>Payment Received</th>
<th>Projected Payments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corn</td>
<td>$73.46</td>
<td>$82.06</td>
</tr>
<tr>
<td>Soybeans</td>
<td>$23.06</td>
<td>$49.46</td>
</tr>
<tr>
<td>Wheat</td>
<td>$17.24</td>
<td>$31.77</td>
</tr>
<tr>
<td>Corn</td>
<td>$0.00</td>
<td>$9.98</td>
</tr>
<tr>
<td>Soybeans</td>
<td>$0.00</td>
<td>$0.00</td>
</tr>
<tr>
<td>Wheat</td>
<td>$0.00</td>
<td>$28.10</td>
</tr>
</tbody>
</table>
Government farm program payments to farm producers, 2009-19F

$ billion (nominal)

Note: F = forecast.
1/ All other payments include supplemental and ad hoc disaster assistance, tobacco transition, Cotton Ginning Cost Share, dairy, and miscellaneous programs (such as the Market Facilitation Program).
2/ Includes Price Loss Coverage (PLC), Agriculture Risk Coverage (ARC), counter-cyclical payments (CCP), Average Crop Revenue Election (ACRE) payments, loan deficiency payments (excluding grazeout payments), marketing loan gains, and certificate exchange gains. CCP and ACRE were not continued in the 2014 Farm Bill. PLC and ARC payments began in 2015.
3/ Includes direct fixed payments portion of Direct and Counter-Cyclical Program (DCP) and Cotton Transition Assistance Program (CTAP) payments (in 2014/15).

2018 Market Facilitation Payments

2018 Market Facilitation Payments by Acre - Ohio
Adjusted to be comparable to 2019 MFP per Acre Rates*

Dollars Per Acre

*calculated by weighting 2018 commodity-specific acreage and multiplying by 2018 yield and 2018 MFP payment rate. Lucas County is divided into East and West, but averaged for this analysis.

Source: USDA Farm Service Agency
Lucas County is divided into East and West, but averaged for this analysis.

2019 Market Facilitation Payments by Acre - Ohio
Only 50% of the County Rate has been Authorized

Dollars Per Acre

CFAES
THE Ohio State University
COLLEGE OF FOOD, AGRICULTURAL, AND ENVIRONMENTAL SCIENCES
2018 Market Facilitation Payments by Acre - Ohio

Adjusted to be comparable to 2019 MFP per Acre Rates*

Dollars Per Acre

*calculated by weighting 2018 commodity specific acreage and multiplying by 2018 yield and 2018 MFP payment rate

Lucas County is divided into East and West, but averaged for this analysis
2019 Market Facilitation Payments by Acre - Ohio
Only 50% of the County Rate has been Authorized

Dollars Per Acre
- Less than $20
- $20-$39
- $40-$59
- $60-$79
- Above $80

Source: USDA Farm Service Agency
Lucas County is divided into East and West, but averaged for this analysis
Taxation of Government Payments  p. 562

• Include in income the year received
  • ARC & PLC payments are for previous year’s production
  • Dairy payment is for current year’s production
• Schedule F (Form 1040)
• Subject to SE tax
Commodity Credit Corporation CCC Loans

- Low interest loan secured by farmer’s unsold crop
- Not included in income unless section 77 election
  - Pay attention to previous years’ election
- If section 77 election, sets crop basis at loan rate
- Example 14.4 provides a good example
Conservation Programs

• Conservation Reserve Program (CRP)
• Conservation Reserve Enhancement Program (CREP)
• Farmable Wetlands Program (FWP)
• Biomass Crop Assistance Program (BCAP)
• Noninsured Crop Disaster Program (NAP)
• Agricultural Management Assistance (AMA)
• Clear 30 – pilot program to benefit water resources
• Soil Health and Income Protection Program (SHIPP)
Include in income
- Usually subject to SE tax
  - Unless material participating farmer receiving Social Security or Disability benefits

IRC § 175 Deduction
- Deduct qualifying soil and water conservation expense

IRC § 126 Exclusion of cost-share payments
- See qualifying criteria in the book (p 566)
Hemp Production

- Legalizes production of hemp removing it from the list of controlled substances
- Unlike marijuana, hemp producers will be able to deduct expenses like typical crops.
- Stay updated on changes at farmoffice.osu.edu
Recent natural disasters, trade disputes, and tax code changes have impacted tax planning for farmers. This issue reviews several tax rules that may help farmers and their professionals plan for 2019 and beyond.
Crop Insurance and Disaster Payments
p. 578

- Cash basis farmers can defer income, planning is important.
  - Deferral election applies to destruction or damage to crops that results in an insurance or disaster payment.
  - Establish that under normal business practice, income from crops would have been reported in following year.
    - Rev. Rul. 74-145 requires taxpayer to show that more than 50% of income from each damaged crop(s) would be reported in the following year.
Making the election pp. 580-581

- Name and address of taxpayer
- Declaration of election under section 451(f)
- ID specific crops damaged or lost
- Declaration of normal business practice
- Cause of loss or damage
- Total payments received
- Name of insurance carrier
Revenue Protection Insurance

- To make the election the payment must be due to destruction or damage of crop(s).
- Revenue policies paying due to income reduction unrelated to such damage do not qualify.

This Photo by Unknown Author is licensed under CC BY-SA
Sofia lost corn crop due to flood.

**FIGURE 14.4 Sofia Diaz’s Revenue Protection Policy Payments—$4.10 Harvest Price**

<table>
<thead>
<tr>
<th>Indemnity payment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Approved yield</td>
</tr>
<tr>
<td>Coverage level</td>
</tr>
<tr>
<td>Base price</td>
</tr>
<tr>
<td>Harvest price</td>
</tr>
<tr>
<td>Actual yield</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Guaranteed amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>180 bushels × $4.00 base price × 65% coverage level × 300 acres</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Calculated revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>50 bushels × $4.10 harvest price × 300 acres</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Insurance payment</th>
</tr>
</thead>
<tbody>
<tr>
<td>$ 78,900</td>
</tr>
</tbody>
</table>
Ex. 14.21 Allocating payments Deferral is Limited  p. 582

Facts same, except price is $3.50

Deferrable amount is $83,320 (cannot claim price loss portion)
  • See calculation in text (94.79% is due to yield loss)

<table>
<thead>
<tr>
<th></th>
<th>Indemnity payment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Approved yield</td>
<td>180 bushels per acre</td>
</tr>
<tr>
<td>Coverage level</td>
<td>65%</td>
</tr>
<tr>
<td>Base price</td>
<td>$4.00</td>
</tr>
<tr>
<td>Harvest price</td>
<td>$3.50</td>
</tr>
<tr>
<td>Actual yield</td>
<td>50 bushels per acre</td>
</tr>
<tr>
<td>Guaranteed amount</td>
<td>$140,400</td>
</tr>
<tr>
<td>Calculated revenue</td>
<td>( 52,500)</td>
</tr>
<tr>
<td>Insurance payment</td>
<td>$ 87,900</td>
</tr>
</tbody>
</table>
I.R.C. § 1033 (e) – the sale or exchange of livestock (other than poultry) held by a taxpayer for draft, breeding, or dairy purposes in excess of the number the taxpayer would sell if he followed his usual business practices shall be treated as an involuntary conversion.

Deferred 2 years unless Federal Disaster than 4 years
Weather-Related Sales of Livestock  p. 582

- I.R.C. § 451(g) – proceeds from livestock sold due to drought, flood, or other weather-related causes deferred 1 year
- For section 451(g) to apply, the livestock does not have to be raised or sold in the weather-related disaster area.
- The taxpayer must show the sale occurred due to the weather-related conditions.
- Cash basis taxpayer whose principle Trade or Business is farming in area that is eligible for federal assistance
Making the election

Attach a statement to return

- Evidence of weather-related conditions
- Compute amount of realized gain
- Number and kind of livestock sold
- Number and kind that would have been sold under normal conditions
- Ex. 14.22 and 14.23
- See Cross-Reference p.586
<table>
<thead>
<tr>
<th>Income Item</th>
<th>Claimed or Deferred</th>
</tr>
</thead>
<tbody>
<tr>
<td>Prevented Planting Indemnity Payments</td>
<td>Can be deferred if history of $&lt; 50%$ crop sales deferred</td>
</tr>
<tr>
<td>Market Facilitation Payments</td>
<td>Must be claimed</td>
</tr>
<tr>
<td>NRCS Cost-Share Payments</td>
<td>Must be claimed</td>
</tr>
<tr>
<td>Farm Bill Program Payments</td>
<td>Must be claimed</td>
</tr>
<tr>
<td>Revenue Insurance Payments</td>
<td>Portion due to low prices must be claimed, portion from low yields can be deferred</td>
</tr>
</tbody>
</table>
As agriculture production has shifted to fewer, larger farms across the United States, the number of smaller farms is also increasing. While taxpayers may engage in farming activities such as beekeeping or growing vegetables for a profit, often these activities are pursued primarily for personal use or benefit. If a taxpayer is engaged in an activity for pleasure, recreation, or even community betterment, the activity is not a trade or business, but is a hobby.
Cost Recovery Planning

- Recognize income instead of deferring to future year
- Slow down depreciation (Section 179 & Bonus Depreciation)
- Perhaps reduce prepayments
- Don’t use de minimis safe harbor for tangible property
- Capitalize rather than expense fertilizer
- Contribute to a Roth, or covert traditional IRA to a Roth
- Take out a CCC loan and treat as income
- Sell grain or livestock to increase income
No Like Kind Exchange for Personal Property

- §1031 now only applies to real property (land) under the TCJA. Farm equipment not eligible.
- Equipment trade-ins are now immediate (in the year) taxable events.
- Most likely result will be taxable gain.
- Taxable gain may be offset – Bonus Dep. & §179
Tractor Trade-In: Old vs. New Rules

2019

New Tractor Cost- $300,000
Tractor for Trade In Value (no tax basis) $200,000
Boot $100,000

Old rules: No gain recognized and no tax due, $100K expensable
New rules: Taxable gain of $200k, $300k expensable
Cautions/Observations

- Some taxpayers may not always be able to immediately offset the gain recognized by taxable exchanges.
- May already have used the maximum $1,000,000 section 179 deduction or may have exceeded the $2,500,000 investment limit on qualifying purchases.
- May not want to use bonus depreciation because it applies to the entire recovery class basis. This may create more than the optimal amount of depreciation expense.
- State taxes will be treated differently – Bonus Dep. And Section 179 have limitations on Ohio state taxes
## No Like Kind Exchange for Personal Property Impacts on State and School District Income Tax

<table>
<thead>
<tr>
<th>Ohio Farmer - Actuals</th>
<th>New Purchase</th>
<th>Trade-In</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equipment</td>
<td>List Price</td>
<td>Value</td>
</tr>
<tr>
<td>JD Sprayer</td>
<td>$533,425</td>
<td>$360,000</td>
</tr>
<tr>
<td>JD 1770NT Planter</td>
<td>$254,224</td>
<td>$198,300</td>
</tr>
<tr>
<td>JD 1795 SR Planter</td>
<td>$289,632</td>
<td>$165,200</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$1,077,281</strong></td>
<td><strong>$723,500</strong></td>
</tr>
</tbody>
</table>

Sec 179 Exp $723,500
Add Back $(5/6 \times (723500 - 25000) = 582083
Allowable Dep. Ohio $141,417
Ohio Taxable Income $582,083
Potential Ohio Tax Due @ 4.797% $27,923
Potential School Tax Due @ 1.5% $8,731
Issue 7: QBI Deduction for Sales to Cooperatives

199A(a) QBI Deduction

199A(b)(7) QBI Deduction Reduction
  • Applies only to Specified Cooperatives and Patrons

199A(g) (New DPAD)
  • Applies only to Specified Cooperatives and Patrons
Need to Segregate Income/Expenses

- Sales to Non-Cooperatives
- Sales to Cooperatives
Sales to Cooperatives
Sales to Cooperatives

- **Step 1:** First, patrons calculate the 20 percent 199A QBI deduction that would apply if they had sold the commodity to a non-cooperative. But they don’t stop there.
- **Step 2:** The patron must then subtract from that initial 199A deduction amount whichever of the following is smaller:
  - 9 percent of net income attributable to cooperative sale(s) OR
  - 50 percent of W-2 wages they paid to earn that income from the cooperative
- **Step 3:** Add back in cooperative's qualified production activities income (QPAI) attributable to that patron's sales. §199A(g) (new DPAD)
### FIGURE 14.17 Calculation of Ben Dover’s QBI Deduction

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Schedule F (Form 1040) gross income</td>
<td>$530,000</td>
</tr>
<tr>
<td>Schedule F (Form 1040) expenses (including W-2 wages)</td>
<td>(480,000)</td>
</tr>
<tr>
<td>Qualified business income</td>
<td>$50,000</td>
</tr>
<tr>
<td>Preliminary QBI deduction ($50,000 × 20%)</td>
<td>$10,000</td>
</tr>
<tr>
<td>Reduction to preliminary deduction is lesser of</td>
<td></td>
</tr>
<tr>
<td>9% of qualified business income ($50,000 × 9%)</td>
<td>$4,500</td>
</tr>
<tr>
<td>50% of W-2 wages ($50,000 × 50%)</td>
<td>$25,000</td>
</tr>
<tr>
<td>QBI deduction</td>
<td>$5,500</td>
</tr>
<tr>
<td>Pass-through § 199A(g) deduction</td>
<td>2,500</td>
</tr>
<tr>
<td><strong>Total QBI deduction</strong></td>
<td><strong>$8,000</strong></td>
</tr>
</tbody>
</table>
Example 14.40 QBI reduction w/o wages

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Schedule F (Form 1040) gross income</td>
<td>$530,000</td>
</tr>
<tr>
<td>Schedule F (Form 1040) expenses (including W-2 wages)</td>
<td>$(480,000)</td>
</tr>
<tr>
<td>Qualified business income</td>
<td>$50,000</td>
</tr>
<tr>
<td>Preliminary QBI deduction ($50,000 x 20%)</td>
<td>$10,000</td>
</tr>
<tr>
<td>Reduction to preliminary deduction is lesser of</td>
<td></td>
</tr>
<tr>
<td>9% of qualified business income ($50,000 x 9%)</td>
<td>$4,500</td>
</tr>
<tr>
<td>50% of W-2 wages ($0 x 50%)</td>
<td>$0</td>
</tr>
<tr>
<td>QBI deduction</td>
<td>$10,000</td>
</tr>
<tr>
<td>Pass-through § 199A(g) deduction</td>
<td>$2,500</td>
</tr>
<tr>
<td>Total QBI deduction</td>
<td>$10,500</td>
</tr>
</tbody>
</table>
Additional Expenses

Taxpayer must include these deductions in the QBI calculation before QBI deduction from specified cooperatives

• Half SE Tax
• SE Health Insurance
• Deduction for contributions to qualified retirement plans
Example 14.41 Cont.

**FIGURE 14.18 Calculation of Ben’s QBI Deduction with Additional Expenses**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Schedule F (Form 1040) gross income</td>
<td>$530,000</td>
</tr>
<tr>
<td>Schedule F (Form 1040) expenses (including W-2 wages)</td>
<td>(480,000)</td>
</tr>
<tr>
<td>Additional expenses ($3,532 + $3,500 + $18,000)</td>
<td>(25,032)</td>
</tr>
<tr>
<td>Qualified business income</td>
<td>$24,968</td>
</tr>
<tr>
<td>Preliminary QBI deduction ($24,968 x 20%)</td>
<td>$4,994</td>
</tr>
<tr>
<td>Reduction to preliminary deduction is lesser of</td>
<td></td>
</tr>
<tr>
<td>9% of qualified business income ($24,968 x 9%)</td>
<td>$2,247</td>
</tr>
<tr>
<td>50% of W-2 wages ($0 x 50%)</td>
<td>0 (0)</td>
</tr>
<tr>
<td>QBI deduction</td>
<td>$4,994</td>
</tr>
<tr>
<td>Pass-through § 199A(g) deduction</td>
<td>2,500</td>
</tr>
<tr>
<td>Total QBI deduction</td>
<td>$7,494</td>
</tr>
</tbody>
</table>
Allocating When Selling to Both

Sales to Non-Cooperatives

Sales to Cooperatives

p 613-615
If Taxpayer has qualified payments from cooperatives (reduce QBI) and other income that is not a qualified payment in its trade or business, the patron must allocate those items and related deductions.

Use reasonable method or safe harbor method.

May allocate by ratably apportioning business expenses based on the proportion that the amount of qualified payments bears to the total gross receipts used to determine QBI.

The same proportion applies to allocate the proper amount of W-2 wages to the portion of QBI comprising qualified payments (that portion for which a reduction must be calculated).
Allocate expenses

• 50/50
• Co-op sales $80,000
• Non-cooperative sales $80,000
• Total expenses $75,000 (including wages)

FIGURE 14.20 Janet Granger’s 2019 Income and Expenses

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Patronage dividends</td>
<td>$80,000</td>
</tr>
<tr>
<td>Sales to a noncooperative grain merchandiser</td>
<td>$80,000</td>
</tr>
<tr>
<td>Total expenses (including W-2 wages)</td>
<td>$75,000</td>
</tr>
</tbody>
</table>

Under the safe harbor allocation, Janet allocates her expenses 50% ($80,000 patronage dividends + $160,000 total sales) to the cooperative and 50% to the noncooperative.
### FIGURE 14.19 Archie Holland’s QBI Deduction with Safe Harbor Allocation

<table>
<thead>
<tr>
<th>Percentage of total income</th>
<th>Total Business Income</th>
<th>Nonqualified Payments</th>
<th>Qualified Payments</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>3.57%</td>
<td>96.43%</td>
<td></td>
</tr>
<tr>
<td>Schedule F (Form 1040) gross income</td>
<td>$280,000</td>
<td>$10,000</td>
<td>$270,000</td>
</tr>
<tr>
<td>Schedule F (Form 1040) expenses</td>
<td>(200,000)</td>
<td>(7,140)</td>
<td>(192,860)</td>
</tr>
<tr>
<td>One-half of SE tax</td>
<td>(5,652)</td>
<td>(202)</td>
<td>(5,450)</td>
</tr>
<tr>
<td>Self-employed health insurance</td>
<td>(12,000)</td>
<td>(428)</td>
<td>(11,572)</td>
</tr>
<tr>
<td>Net qualified business income</td>
<td>$62,348</td>
<td>$2,230</td>
<td>$60,118</td>
</tr>
</tbody>
</table>

Preliminary QBI deduction (20% x QBI) | $446 | $12,024 |

Reduction is lesser of:
- 9% of qualified business income | N/A | $5,411 |
- 50% of wages | N/A | $4,822 |
- QBI deduction (20% of QBI – lesser of 9% of qualified business income or 50% of wages) | N/A | $7,202 |

QBI deduction | $446 | $7,202 |
199A(g) Deduction

Co-op must send notice to taxpayer

- The “New DPAD”
- For specified coops and their patrons
- Pass through some or all of the deduction
Farmers making the decision to cease the farming business either voluntarily by retiring or involuntarily through financial distress may face significant tax liabilities.

Generally, sale of all the farm assets within the same tax year will result in the highest tax liability for the farmer who chooses to go out of business.

Are you having these conversations with your farm clientele?
### Gain calculation of total sale

<table>
<thead>
<tr>
<th>Asset</th>
<th>FMV</th>
<th>Basis</th>
<th>Gain (loss)</th>
<th>Character</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stored grain</td>
<td>$50,000</td>
<td>$0</td>
<td>$50,000</td>
<td>Ordinary</td>
</tr>
<tr>
<td>Livestock held for sale</td>
<td>100,000</td>
<td>20,000</td>
<td>80,000</td>
<td>Ordinary</td>
</tr>
<tr>
<td>Real property</td>
<td>480,000</td>
<td>210,000</td>
<td>270,000</td>
<td>Long-term capital gain (section 1231)</td>
</tr>
<tr>
<td>Equipment</td>
<td>100,000</td>
<td>0</td>
<td>100,000</td>
<td>Ordinary (section 1245)</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$730,000</strong></td>
<td><strong>$230,000</strong></td>
<td><strong>$500,000</strong></td>
<td></td>
</tr>
</tbody>
</table>
Ordinary tax $46,944
LTCG triggers tax $43,773
Total tax bill $90,717

George nets $639,283, BUT he still owes the bank $60,717
Selling over Several Years    p. 602

Ex. 14.32, same facts as Ex. 14.31, but George sells over time, tax bill is reduced by $15,061 ($90,717 − $75,656)

Does not address net present value of money, additional interest paid, change in valuation of assets over time, etc. It may be advisable to sell in one year even with insufficient income to cover the loan.
FIGURE 14.16 George’s Tax Liability—Selling Assets over Several Years

<table>
<thead>
<tr>
<th></th>
<th>Total Gain (Loss)</th>
<th>2019</th>
<th>2020</th>
<th>2021</th>
<th>2022</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stored grain</td>
<td>$ 50,000</td>
<td>$ 50,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Livestock held for sale</td>
<td>80,000</td>
<td></td>
<td>$80,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Real property</td>
<td>270,000</td>
<td>270,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equipment</td>
<td>100,000</td>
<td></td>
<td></td>
<td>$50,000</td>
<td>$50,000</td>
</tr>
<tr>
<td>Total gain (loss)</td>
<td>$500,000</td>
<td>$320,000</td>
<td>$80,000</td>
<td>$50,000</td>
<td>$50,000</td>
</tr>
<tr>
<td>Other income</td>
<td>5,000</td>
<td>5,000</td>
<td></td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Total taxable income</td>
<td>$505,000</td>
<td>$325,000</td>
<td>$80,000</td>
<td>$50,000</td>
<td>$50,000</td>
</tr>
</tbody>
</table>

| Tax liability\(^1,2,3,4\) | $75,656          | $48,464 | $13,464 | $6,864 | $6,864 |

---

1. 2019: Capital gain: $270,000 × 15% = $40,500
2. 2019: Ordinary income = $5,000 + $50,000 = $55,000; tax liability using tax tables = $7,964
3. 2020: Ordinary income = $80,000; tax liability using tax tables = $13,464
4. 2021, 2022: Ordinary income = $50,000; tax liability using tax tables = $6,864
Installment Sale Option

Taxpayers can use the installment method by taking payments over time.

- Installment reporting is automatic if:
  - There is gain on the sale
  - At least one payment received in year after sale
  - Gain is not from depreciation recapture (§ 1245 gain)
Issue 1: Qualified Conservation Contributions  

Deduction Limitation

- 50% of AGI for average taxpayer
- 100% of AGI for qualified farmer or rancher
- Reported on Schedule A, Itemized Deductions
  - Remember higher standardized deduction levels so $ amount matters
- Unused deduction carried forward up to 15 years

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Approved Conservation Purposes p. 553-556

- Recreation or Education
- Protection of Environmental Systems
- Preservation of Open Spaces
- Historical Preservation
Valuation of Contributed Property  pp. 558-559

- Usually difference between FMV w/out restriction and FMV w/ restriction
- See Example 14.3
- No tax deduction if grant does not decrease FMV (Wendell)
Issue 3: Oil and Gas

There are often several different streams of income generating from utility easements. This section focuses on oil and gas, but renewable energy can generate similar issues.
Temporary Easement Payments

Temporary easement for constructing a pipeline (treated as a rental payment)
Payment reported on Sch E (Form 1040)
Payment not subject to SE Tax
Permanent Easement Payments

- Permanent easement treated as sale of land
- Rev. Rul. 72-255, 1972-1 C.B. 221
- Sale of an easement – determining basis
- Treas. Reg. § 1.61-6(a):
  - Basis is allocated among the parts
  - Separate transactions
  - Gain or loss is not deferred
  - Report on Form 4797
Damage Payments

Crop damage
- Ex 14.6 – treated as sale of crop

Soil compaction or land damage
- Ex. 14.7 – recovery of capital and reduce basis

Tile damage is often repaired by company
Issue 5: C Corp conversion to S Corp pp. 596 - 601

- QBI deduction of 20% of qualified income is not allowed for C corps. With a flat tax rate of 21%, and a tax on dividends, converting to an S Corp may be of interest.

- Looking long term: the 21% flat tax rate is permanent while the 20% QBID is set to expire after 2025. What will congress do in the future?

- Is this an issue you are seeing?
"Well, don't just sit there — Go out and earn some more money!"
Thank You!

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