



Farm Income Taxes & Records

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Income Tax Disclaimer



All information provided is considered educational and not legal or tax advice. I am not a CPA or income tax accountant. Specific tax issues related to your situation or farming operation should be discussed with a well-trained tax preparer or CPA.

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Public Service Announcement



**Know what's below.
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Taxes and Records



- Better records makes it easier for your tax preparer to do a more accurate job in preparing your tax return
- Good records may reduce the cost of tax return preparation
- Seek a CPA / tax preparer who understands farming
- Best record keeping system = one you will use!
- More on record keeping later.

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Today's Tax Topics



- Current Tax Issues
- Depreciation (+ Bonus Depreciation & Section 179)
- Reporting Livestock Sales - correctly
- Sole proprietorship, Partnership & Qualified Joint Venture
- What are auditors looking for? (hobby farms)
- Like-kind Exchanges
- Qualified Business Income Deduction (QBID)
- Tax Reducing Tips
- Net Operating Loss
- Greenbelt and Ag Sales Tax Exemption
- Estate Tax Exemption Update
- IRS and 401K beneficiary rules update

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Current Tax Issues



- Standard Deduction: Single-\$12,550, MFJ- \$25,100, HOH- \$18,800
- Tax Rates: 10% (up to \$9,950 single, \$19,900 MFJ),
12% (up to \$40,525 single, \$81,050 MFJ),
22% (up to \$86,375 single, \$172,750 MFJ)
24%, 32%, 35%, 37%
- Charitable giving/Donation \$300 per person (\$600 MFJ)
- Child Tax credit \$3,000 or \$3600 (under age 6)
 - \$250 or \$300 per month July-Dec 2021 (remainder when taxes filed)

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Depreciation



- **New Equipment – 5 years, Used - 7 years**
- **Bonus Depreciation 100% through 2022, 80%-2023, 60%-2024.....**
 - New equipment (maybe used), for all equipment in a recovery class
- **Section 179 Deduction—on per item basis, max \$1,020,000, cannot create loss**
- **Depreciation table**

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Farm Asset Recovery Periods – by GDS Class

October 2020

Asset	GDS Life	ADS Life	Method	Sec 179
Hogs (breeding)	3	3	200% DB	Yes
Tractor units (over-the-road)	3	4	200% DB	Yes
Autos	5	5	200% DB	Yes
Calculators and Copiers	5	6	200% DB	Yes
Cattle (dairy or breeding)	5	7	200% DB	Yes
Computer and peripheral equipment	5	5	200% DB	Yes
New farm machinery and equipment ¹	5	10	200% DB	Yes
Goats and sheep (breeding)	5	5	200% DB	Yes
Logging machinery and equipment ²	5	6	200% DB	Yes
Truck (heavy duty, unloaded weight 13,000 lbs. or more)	5	6	200% DB	Yes
Truck (actual weight less than 13,000 lbs.)	5	5	200% DB	Yes
Communication equipment ³	7	10	200% DB	Yes
Used farm machinery and equipment	7	10	200% DB	Yes
Fences (agricultural)	7	10	200% DB	Yes
Grain bin	7	10	200% DB	Yes
Horses (age when placed in service)				
Breeding and working (12 years or less)	7	10	200% DB	Yes
Breeding and working (more than 12 years)	3	10		
Racing horses (more than 2 years)	3	12		
Office furniture, fixtures and equipment	7	10	200% DB	Yes
Agricultural and Horticultural Single Purpose Structure	10	15	200% DB	Yes
Horticultural structures (single purpose)	10	15	200% DB	Yes
Trees or vines bearing fruit or nuts	10	20	SL	Yes
Drainage facilities	15	20	150% DB	Yes
Paved Lots	15	20	150% DB	Yes
Water wells	15	20	150% DB	No
Farm Buildings ⁴	20	25	150% DB	No
Residential rental property	27.5	40	SL	No
Nonresidential real property	39 ⁵	40	SL	No

Footnotes:

1 Not including grain bin, cotton ginning, asset fence, or other land improvements and the original use starts with you and placed in service after December 31, 2017.

2 Used by logging and sawmill operators for cutting of timber

3 Not including communication equipment listed in other classes

4 Not including single purpose agricultural and horticultural structures

5 For property placed in service after May 12, 1993.

Depreciation - continued



- **Small equipment under \$2500 can be expensed**
- **Purchase of asset should not be based on a need for depreciation**
- **Can a new asset increase income or reduce labor and expenses?**

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Types of Livestock Sales



- **Two major types: Calves or Breeding Livestock**
- **Calves = Raised or Purchased (and resold)**
- **Breeding Livestock = Animals raised or purchased for the purpose of breeding**
- **Heifers, Cows and Bulls – Raised or Purchased**
- **Extension Publication D42 – Livestock Sales – Understanding Tax Impacts**

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SCHEDULE F (Form 1040)		Profit or Loss From Farming		OMB No. 1545-0074 2020 Attachment Sequence No. 14	
Department of the Treasury Internal Revenue Service (99)		Attach to Form 1040, Form 1040-SR, Form 1040-NR, Form 1041, or Form 1065. Go to www.irs.gov/ScheduleF for instructions and the latest information.		Social security number (SSN)	
Name of proprietor		Accounting method: <input type="checkbox"/> Cash <input type="checkbox"/> Accrual		Employer ID number (EIN) (see instr.)	
A Principal crop or activity		B Enter code from Part IV		D Did you "materially participate" in the operation of this business during 2020? If "No," see instructions for limit on passive losses.	
				<input type="checkbox"/> Yes <input type="checkbox"/> No	
E Did you make any payments in 2020 that would require you to file Form(s) 1099? See instructions.				<input type="checkbox"/> Yes <input type="checkbox"/> No	
F If "Yes," did you or will you file required Form(s) 1099?				<input type="checkbox"/> Yes <input type="checkbox"/> No	
Part I Farm Income—Cash Method. Complete Parts I and II. (Accrual method. Complete Parts II and III, and Part I, line 9.)					
1a Sales of livestock and other resale items (see instructions)		1a		1c	
b Cost or other basis of livestock or other items reported on line 1a		1b		2	
c Subtract line 1b from line 1a				2	
2 Sales of livestock, produce, grains, and other products you raised				3b Taxable amount	
3a Cooperative distributions (Form(s) 1099-PATR)		3a		3b Taxable amount	
4a Agricultural program payments (see instructions)		4a		4b Taxable amount	
5a Commodity Credit Corporation (CCC) loans reported under election		5a		5a	
b CCC loans forfeited		5b		5c Taxable amount	
6 Crop insurance proceeds and federal crop disaster payments (see instructions):				6b Taxable amount	
a Amount received in 2020		6a		6b Taxable amount	
c If election to defer to 2021 is attached, check here <input type="checkbox"/>				6d Amount deferred from 2019	
7 Custom hire (machine work) income				7	
8 Other income, including federal and state gasoline or fuel tax credit or refund (see instructions)				8	
9 Gross income. Add amounts in the right column (lines 1c, 2, 3b, 4b, 5a, 5c, 6b, 6d, 7, and 8). If you use the accrual method, enter the amount from Part III, line 50. See instructions.				9	
Part II Farm Expenses—Cash and Accrual Method. Do not include personal or living expenses. See instructions.					
10 Car and truck expenses (see instructions). Also attach Form 4562		10		23 Pension and profit-sharing plans	
11 Chemicals		11		24 Rent or lease (see instructions):	
12 Conservation expenses (see instructions)		12		a Vehicles, machinery, equipment	
13 Custom hire (machine work)		13		b Other (land, animals, etc.)	
14 Depreciation and section 179 expense (see instructions)		14		25 Repairs and maintenance	
15 Employee benefit programs other than on line 23		15		26 Seeds and plants	
16 Feed		16		27 Storage and warehousing	
17 Fertilizers and lime		17		28 Supplies	
18 Freight and trucking		18		29 Taxes	
19 Gasoline, fuel, and oil		19		30 Utilities	
20 Insurance (other than health)		20		31 Veterinary, breeding, and medicine	
21 Interest (see instructions):				32 Other expenses (specify):	
a Mortgage (paid to banks, etc.)		21a		a	
b Other		21b		b	
22 Labor hired (less employment credits)		22		c	
				d	
				e	
				f	
33 Total expenses. Add lines 10 through 32f. If line 32f is negative, see instructions.		33		32a	
34 Net farm profit or (loss). Subtract line 33 from line 9. If a profit, stop here and see instructions for where to report. If a loss, complete lines 35 and 36.		34		32b	
				32c	
				32d	
				32e	
				32f	
35 Reserved for future use.					
36 Check the box that describes your investment in this activity and see instructions for where to report your loss:					
a <input type="checkbox"/> All investment is at risk.		b <input type="checkbox"/> Some investment is not at risk.			

Part I Farm Income—Cash Method. Complete Parts I and II. (Accrual method. Complete Parts II and III, and Part I, line 9.)					
1a Sales of livestock and other resale items (see instructions)		1a		1c	
b Cost or other basis of livestock or other items reported on line 1a		1b		2	
c Subtract line 1b from line 1a				2	
2 Sales of livestock, produce, grains, and other products you raised				3b Taxable amount	
3a Cooperative distributions (Form(s) 1099-PATR)		3a		3b Taxable amount	
4a Agricultural program payments (see instructions)		4a		4b Taxable amount	
5a Commodity Credit Corporation (CCC) loans reported under election		5a		5a	
b CCC loans forfeited		5b		5c Taxable amount	
6 Crop insurance proceeds and federal crop disaster payments (see instructions):				6b Taxable amount	
a Amount received in 2020		6a		6b Taxable amount	
c If election to defer to 2021 is attached, check here <input type="checkbox"/>				6d Amount deferred from 2019	
7 Custom hire (machine work) income				7	
8 Other income, including federal and state gasoline or fuel tax credit or refund (see instructions)				8	
9 Gross income. Add amounts in the right column (lines 1c, 2, 3b, 4b, 5a, 5c, 6b, 6d, 7, and 8). If you use the accrual method, enter the amount from Part III, line 50. See instructions.				9	

Breeding Livestock



- Tax treatment depends on:
 - Whether animal raised or purchased
 - How long animal was held (owned): cattle or horses owned 24 months or longer = long term
 - Whether sale resulted in a gain or loss
- Sales reported on Form 4797 not Schedule F

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Form **4797**Department of the Treasury
Internal Revenue Service

Sales of Business Property

(Also Involuntary Conversions and Recapture Amounts
Under Sections 179 and 280F(b)(2))

► Attach to your tax return.
► Go to www.irs.gov/Form4797 for instructions and the latest information.

OMB No. 1545-0184

2019Attachment
Sequence No. **27**

Farmers tax Guide (Pub 225) and/or Instructions for Form 4797 explain where on form sales are entered.

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Raised Breeding Livestock



- **Reported on Form 4797 not Schedule F**
- **Example 3.** Farmer C sold a 4-year-old raised cow for \$1,100. The expenses of the sale are \$125, and these are deducted from the gross sales price to arrive at a gain of \$975. This gain is a long-term gain since the cow was held at least two years and is not subject to self-employment tax. This gain would be combined with other gains and losses to determine net gains and losses for the year.

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Purchased Breeding Livestock



- **Reported on Form 4797 not Schedule F**
- **Example 4.** Farmer D sold a cow purchased four years ago. The cow was purchased for \$1,300 and sold for \$1,250. The amount of depreciation taken was \$867, and the expense of the sale was \$125. The gain from the sale of the purchased cow is calculated as follows:

• Gross selling price	\$1,250
• Original cost	\$1,300
• Add expense of sale	+ 125
• Less allowable depreciation	- <u>867</u>
• Adjusted basis	<u>\$ 558</u>
• Gain realized	\$ 692

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Cost of Incorrect Tax Reporting



- If Farmer D had mistakenly reported the sale of the cow for \$1,250 on Schedule F as raised livestock with no basis, the entire amount would be considered ordinary income and would be subject to self-employment tax. Depending on the farmer's adjusted taxable income from all sources, if the farmer is in the 10 percent tax bracket, the overpayment of income tax (10%) and self-employment tax (15.3%) in this case could be about \$300.
- In years when a farm has an overall loss, improper reporting reduces the loss and could increase taxes owed, as less income from other sources (off-farm, investments, etc.) would be offset by the reduced loss.

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Holding Period Rules



- Long-term Capital gain holding period generally is 24 months of cattle and horses and 12 months for other livestock.
- Other important rules:
- There are some exceptions to the holding period rules for situations like weather-related sales of livestock.
- If an animal is raised with the intent to become breeding livestock and it is determined the animal is sterile and the animal is sold within a reasonable time, it could be considered breeding livestock.
- A farmer who is selling an entire herd of animals, generally, could consider the younger animals that would have become breeding livestock as such for tax purposes.

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Livestock Sale Reporting Summary



- **Separate reporting of livestock sales FOUR ways:**
- **Calves raised**
- **Calves purchased**
- **Breeding Livestock raised**
- **Breeding Livestock purchased**

- **Make sure your tax preparer understands!**

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Farm Ownership



- **Sole Proprietor**
- **Partnership – Form 1065**
 - **Spouses may be considered partners by IRS**
- **Qualified Joint Venture**
 - **Filing option for spouses when both involved in farm operation (prevents filing Form 1065)**

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What are Auditors looking for?



- **Proof of Profit Motive**
- **Business / Farm Plan**
- **Separate records / accounts**
- **Continued education/training**
- **Changes / improvements to become profitable**
- **High off-farm income**

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Like Kind Exchange



- **Only Real Estate (land & buildings) qualify – must follow rules carefully**
- **Trade in of equipment – NOT a like kind exchange**
 - Trade in tractor – value of trade-in shown like a sale (may require recapture of depreciation).
 - Generally allows depreciation of full cost of new tractor.
 - Often reduces self-employment taxes.

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QBID

Qualified Business Income Deduction

- Began in 2018, replaced domestic production activities deduction
- Most farms qualify for QBID
- 20% deduction
- No profit = no deduction



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General Farm Tax Reducing Tips

- Prepaying Expenses – Feed, Fertilizer, Seed, etc.
 - Must be purchase not a deposit
- Paying Children under age 18 - no SE tax
- Income Averaging
- Deferring disaster or crop insurance payments-
 - Sale in following year must be normal practice
- Timber sales – establish basis (value) in timber



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Net Operating Loss



- **Maximum \$250,000 single (\$500,000 MFJ)**
- **Farmers allowed 2 year carryback.**
- **Can carry forward indefinitely**
- **NOL Carry forward can offset up to 80% of income**
- **Easier to carry forward**
- **Non farms not allowed carryback**

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Other Tax Issues



- **Property Tax – Greenbelt**
 - **Agricultural, Forest, Open Space land**
 - **15 acres minimum (can be contiguous tracts)**
 - **Avg \$1500 ag income per year (over 3 year period)**
 - **Lowers tax value on land only (not buildings)**
- **Contact County Tax Assessors office**
- **Greenbelt manual:**
[2019.09.30.SBOEGreenbeltManual.pdf \(tn.gov\)](https://www.tn.gov/2019/09/30/SBOEGreenbeltManual.pdf)

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Other Tax Issues



- Agricultural Sales Tax Exemption
- TN Dept of Revenue: [Agricultural Exemption \(tn.gov\)](https://www.tn.gov)
- Form to apply and list of exempted items on website or form available at Extension offices
- Proof of farming: copy of Schedule F or letter describing farm operation for new farms
- Minimum \$1000 of products produced per year

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Farm Type Tax Issues



- Record keeping and tax issues vary based on farm type
- Row Crop – Income, Expenses, equipment, buildings, etc.
- Livestock – above, + breeding animals
- Poultry – above + type of payment (per animal, per square foot (review contract & payment with tax preparer to determine reporting))

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Estate Tax Exemption & IRAs



- **2021 Federal Estate Tax exemption = \$11,700,000**
- **Secure Act passed in 2019 impact:**
- **Retirement accounts – IRA, 401K**
 - **2020 Law Changes!**
 - **Required minimum distribution (RMD) required now at age 72**
 - **Change to beneficiary withdrawal rules**

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Recordkeeping: Why is it important?



- **Good records assist good managers in making more informed business decisions.**
 - Records can be used in creating budgets.
 - Aid in creating accurate financial statements.
 - They allow you to see where your money is going.
 - Help managers answer important questions like:
 - What is our total income?
 - How have numbers changed over the years?
 - Can we be more efficient in our business?

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Financial vs. Production Records



- **Financial records primarily pertain to the income and expense transactions on the farm** (sales, expenses, purchases, etc.)
- **Production records are those items that describe quantities of input items and production measures** (animal ID, birthweights, calving rate, death loss, weaning weights, crop yields, fertilizer & seeding rates, planting and harvesting dates, etc.)

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Financial Records



- A complete set of financial records allow managers to:
 - Know the true cost of production
 - Calculate break even prices
 - Plan for expansion (or reduction) of the business
 - Calculate the availability of cash for loan payments or living costs
 - Determine the profitability of each enterprise
 - Improves working relationship with lenders
 - Help create marketing plans

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Production Records



- Track management decisions
- Verify herd /crop yield improvements
- Aid in culling decisions
- Proof of farm sustainability
- Plan future changes / improvements
- Qualify for government/disaster programs

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Methods of Recordkeeping



- “Shoebox” Method
- Pen and Paper Method
- Spreadsheet: Excel
- Computer program: Quicken and QuickBooks

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Quicken vs QuickBooks



- **Quicken:** is designed for personal finances and works well for most farm operations (easy to learn, looks like a checkbook register)
- **QuickBooks:** is designed for small business accounting platforms, invoicing, payroll, etc. (more of a true accounting program)

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Quicken: Record Keeping Software



- **Quicken parts:**
 - **File:** is the name of where the information is store, ie. Farm Name
 - **Account:** allows for many types - Checking, Savings, Cash, Credit, Investment
 - **Category:** either income or expense, Feed, Seed, Fuel, Utilities, Taxes, Fertilizer, Insurance, etc.
 - **TAG:** different farm enterprises, Corn, Soybeans, Cattle, Pumpkins, Overhead Expenses
 - Many built in reports

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Conclusion



- **Recordkeeping is essential to running a profitable business.**
- **The method of recordkeeping can either make the task burdensome or convenient.**
- **Choose and use the recordkeeping system that best fits your operation and needs!**

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QUESTIONS



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