Managing Taxes Before Year-End

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October 2024

Rural Tax Education

RuralTax.org

Content:

Management strategies
+ / - Expenses
+ / - Revenues
Other options
1099s

Disclaimer

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Disclaimer

- None of what is presented should be considered formal legal or tax advice
- This presentation is for educational purposes
- Consult with trusted professionals on your individual situation

Planning

- It is October and time to evaluate options
- Consult your tax and business management professionals

Planning

- What should or can you do?
- What options are available?
- The goal is to prepare you for discussions with your tax preparer.

A couple notes

- Farming / Schedule F is one part of an overall tax return
- Deferring tax does not eliminate tax but is a tax management tool
- What helps your family and business thrive?

Single Filing Status
2024 tax rate bracket income ranges

- 10% – $1 to $11,600;
- 12% – $11,601 to $47,150;
- 22% – $47,151 to $100,525;
- 24% – $100,526 to $191,950;
- 32% – $191,951 to $243,725;
- 35% – $243,726 to $609,350; and,
- 37% – $609,351 or more.

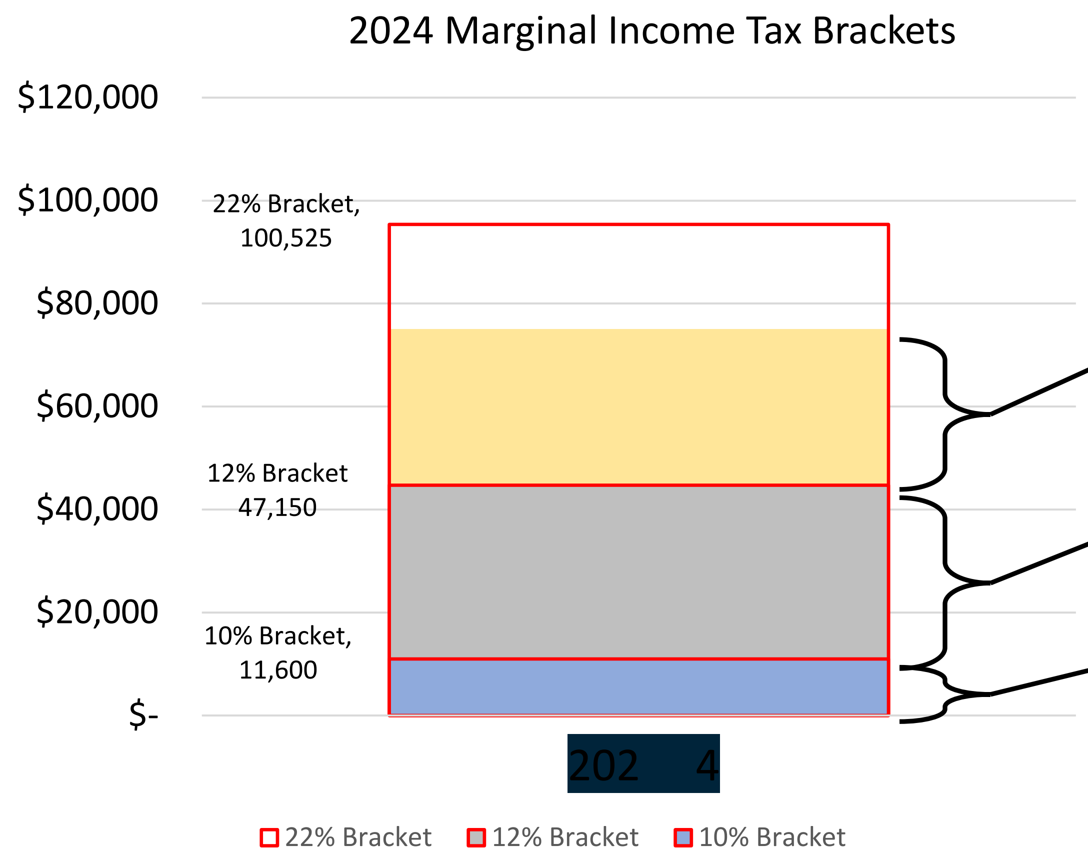
Typically, add 15.3% of net farm income for self-employment tax

Single Filing Status
2025 tax rate bracket income ranges

- 10% – $1 to $11,925;
- 12% – $11,926 to $48,475;
- 22% – $48,476 to $103,350;
- 24% – $103,351 to $197,300;
- 32% – $197,301 to $250,525;
- 35% – $250,526 to $626,350; and,
- 37% – $626,351 or more.

Typically, add 15.3% of net farm income for self-employment tax

Marginal Taxes



Ima Farmer is single and has a taxable federal income of $75,000 for 2024.

	Marginal Taxes
22% Tax Rate for income above $47,150 (75,000 – 47,150 = 27,850)	$6,127
12% Tax Rate for income above $11,600 and below $47,150 (35,550)	$4,266
10% Tax Rate for income up to $11,600	$1,160
	$11,553

Single Filing Status
2024 tax rate bracket income ranges
Taxable Income = $75,000

- 10% – $1 to $11,600; $1,160
- 12% – $11,601 to $47,150; $4,266
- 22% – $47,151 to $100,525; $6,127

Effective Tax Rate = Total Tax ÷ Taxable Income

$11,553 ÷ $75,000 = 15.4% effective tax rate

Tax Planning Strategies

- Minimize income tax owed
  - Prepay expenses, maximize depreciation, defer income
- Optimize after tax income
  - Optimum marginal tax brackets & review effective tax rate

Tax Planning Rule of Thumb

In the long run:

Net farm income + Non-farm income

Should Be Greater Than

Family living expense + Income tax liability + Land principal payments

Tax Planning Caution ⚠

- Equipment purchases should be based on need, not on income tax savings.
- Do not let the tax tail wag the business dog!

Tax Planning

- Ag producers have unique options for income tax planning

  - Many tools or options not available to main street businesses

- Working with your tax professional before year end is your most effective tool

- Leave yourself some wiggle room if possible

- Sometimes, things just happen…

Tools for Tax Planning

- Depreciation options
- Paying for business use items that will not be used until the following year (prepaid expenses)
- Defer reporting income until the following year
- Expensing vs amortizing fertilizer expense
- Installment sale contracts for production

Tax Planning in High Income Years

- Accelerate depreciation (§179 or bonus)
- Accelerating depreciation does not provide more depreciation, it simply changes the timing of the depreciation deduction
- Trade-off between current expense vs. later deduction
- Expense fertilizer purchases v amortizing
- Prepay operating expenses for items to be used next year
- Trade-off between current expense vs. later deduction
- All of these can reduce the amount of current year taxable income

Tax Planning in Low Income Years

- Depreciation tools with a Slower Write-Off
- Amortizing v expensing fertilizer purchases
- Elect out of installment sale contracts for production
- Do not prepay expenses
- All of these can increase the amount of current year taxable income

What is Tax Depreciation

- It is the legal method used to recover the cost of an asset that has a useful life that is greater than 1 year.
- Tax rules vary by asset and whether item is new or used.
  - New Combine = 5-year recovery period
  - Used Combine = 7-year recovery period

Depreciation Options

- Accelerated depreciation (Section 179 Expensing [aka §179] or Additional First Year "Bonus" Depreciation [aka §168]
- Accelerating depreciation does not provide more depreciation, it simply changes the timing of the depreciation deduction
- Trade-off between current year expense vs. a later deduction
- Taking Section 179 or Bonus Depreciation on financed equipment is deducting an expense that has not been paid yet (the depreciation deduction does not match cashflow timing)

§179 Depreciation

- Allows businesses to deduct elected cost of qualifying assets in the first year
- What property qualifies?
  - Used primarily in a trade or business (>50% business use)
  - Acquired by purchase
  - Generally, 15-year tangible personal property or less
  - Machinery & equipment, breeding livestock, single purpose agricultural or horticulture structures, certain business vehicles, computers, software, office furniture

§179 Depreciation Limits

- Maximum deduction limited to $1,220,000 (2024)
- Investment in qualified property limited to $3,050,000 (2024)
  - Each $1 over investment limit reduces deduction limit by $1
  - Investment of $4,270,000 or more = no §179 deduction allowed
- §179 deduction cannot exceed net business income
  - W2 wages, income from farm business (Schedule F), non-farm business (Schedule C), certain pass-through income (Schedule E, page 2), gain on certain business property (Form 4797)

§168 Special Depreciation

- Special "bonus" depreciation allowance is an additional deduction before calculating regular depreciation
  - 60% for 2024, 40% for 2025, 20% for 2026, zero for 2027
- What property qualifies?
  - Tangible personal property with a life of 20-years or less
  - Acquired by purchase
  - Generally, the same assets as with §179 plus farm buildings

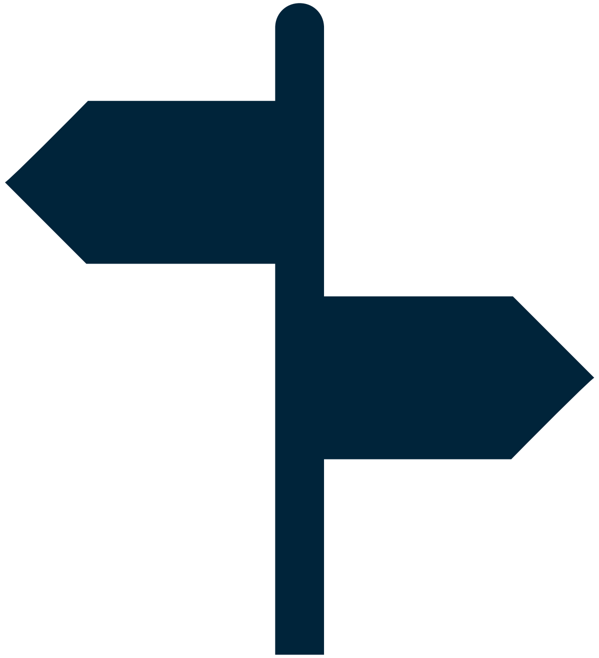
§168 Special Depreciation

- "Bonus" depreciation is default, must elect to not use
  - Election applies to all property within an asset class

- No investment or deduction limits, bonus can create a business loss

§179 vs §168

- §179 allows taxpayer to choose the deduction amount, up to the cost of the property, election made for each eligible asset
- §168 is all-or-none for all property within an asset class
- §168 allowed for farm shops, machine sheds, etc.



Other Depreciation Options

- Elections available to slow down depreciation to reduce depreciation expense and increase taxable income
  - 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)

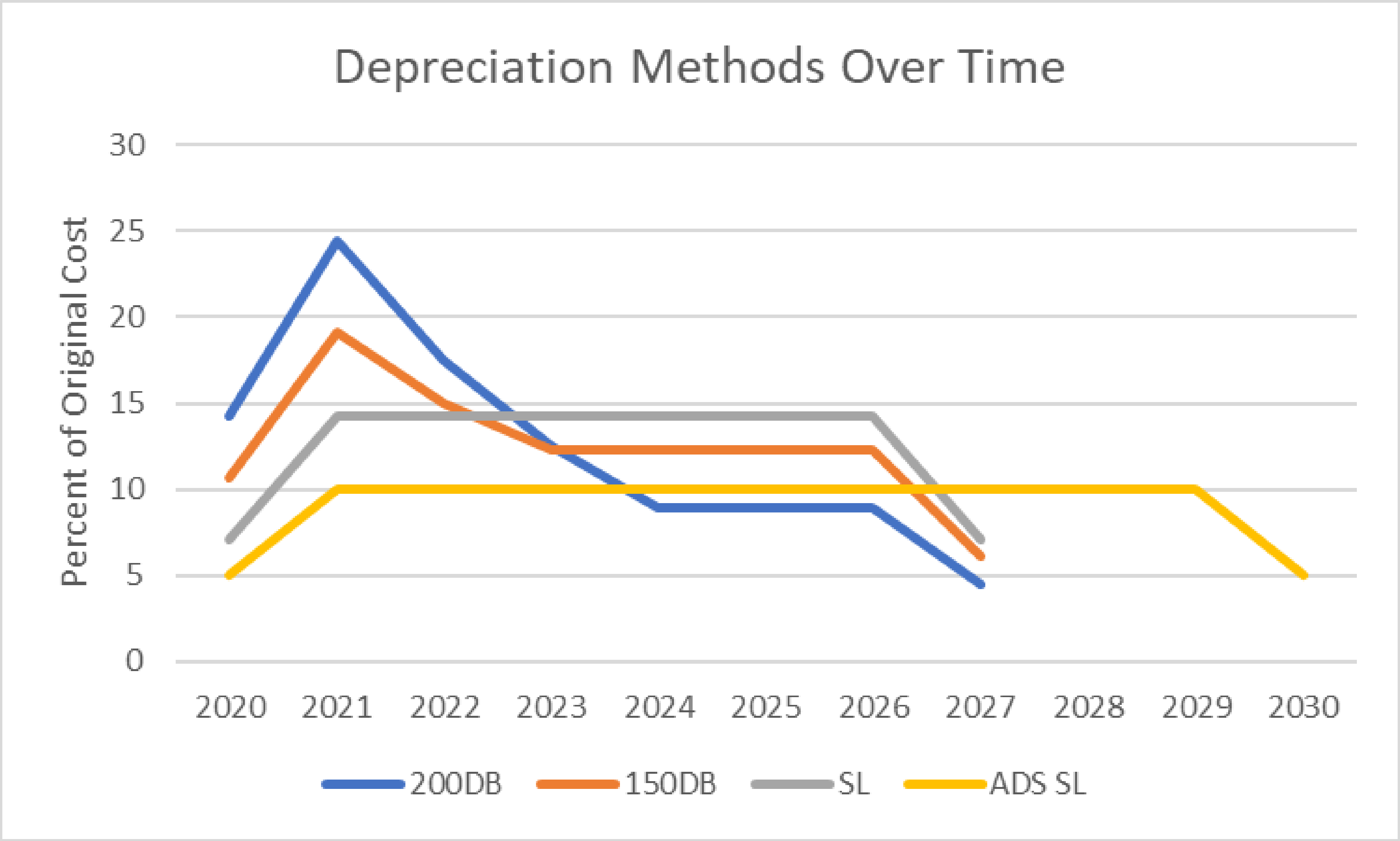
Other Depreciation Options

- IRS Pub 225 page 44

Table 7-1. **Farm Property Recovery Periods**

Assets	Recovery Period in Years	
	GDS	ADS
Agricultural structures (single purpose)	10	15
Automobiles	5	5
Calculators and copiers	5	6
Cattle (dairy or breeding)	5	7
Communication equipment[1]	7	10
Computer and peripheral equipment	5	5
Drainage facilities	15	20
Farm buildings[2]	20	25
New farm machinery and equipment[3]	5	10
Used farm machinery and equipment	7	10
Fences (agricultural)	7	10
Goats and sheep (breeding)	5	5
Grain bin	7	10
Hogs (breeding)	3	3

Other Depreciation Options



Prepaying Farm Expenses

- Amount paid during the current tax year for items that will be used in the following tax year
- Must be a payment; not a deposit
- Must be made for a valid business purpose
- Must not materially distort income
- Works well in a high-income year

Expensing v Amortizing Fertilizer

- Typically, the cost of fertilizer is deducted in the year it is paid for
- Fertilizer may have a benefit for more than just 1 year
- Annual Election can be made to spread cost over its useful life
- Works well in a low-income year

Constructive Receipt

- Constructive receipt is the point when the taxpayer has control of the funds
- You have control of the funds, if you have received a check even if it is not deposited in the bank
- You have control of the funds, if you <u>have the ability</u> to receive a check even if you have not yet received it

Deferred Payment Contract

- Sale of grain or livestock in the current year with a contract for payment sometime in the future (usually the next tax year)
- Written contract with purchaser (elevator or sale barn)
  - Specifies quantity, price, grade, and time of payment in following year
  - Seller has no right to receive the proceeds until the date specified
- Common method of taking advantage of a price but delaying recognition of income
- May be a risk of non-payment as an unsecured creditor

Deferred Payment Contract

- Also referred to as "Installment Sale Contracts for Production"
- Requirements:
  - Must be a bona fide arm's-length contract with the buyer.
  - Seller cannot have any right to the commodity after it is delivered.
  - Must avoid constructive receipt so contract must be in place before delivery.

Deferred Payment Contract

- Option to elect out of installment treatment on deferred payment contracts
  - Recognize income in the year of sale even though payment is not to be received until a future year
  - Effective tax planning tool if there is income uncertainty
  - Election is all or none on a contract-by-contract basis
  - Plan for flexibility by selling multiple contracts in varying amounts
- Works well in a high-income year

Defer Crop Insurance

- Potential to defer crop insurance proceeds, from crop damage or destruction, to the year following production
  - Available if you normally sell > 50% of grain the following year
  - Cash basis taxpayers only
  - If qualified, all crop insurance proceeds must be deferred even if from different crops

- Revenue policies may have both revenue and yield loss coverage
  - Revenue portion of crop insurance cannot be deferred

- Rainfall or weather insurance proceeds cannot be deferred

CCC Loan Election

- Loan from CCC on grain in storage (commercial or home storage)
- Requires work before year end, but allows flexibility after-the-fact
- Election allows loan proceeds to be treated as income
- 2024 National loan rate ($/bushel)

  Wheat= $3.38, Corn= $2.20, Grain Sorghum= $2.20, Soybeans= $6.20
- Requires accurate accounting records

Retirement Plan Contributions

- Traditional IRA contribution
  - Requires earned income to contribute
  - Maximum contribution of $7,000 per individual for 2024 ($8,000 if 50 or older)
  - Maximum contribution may be limited if you, or your spouse, participate in a qualified retirement plan
  - Plan may be established as late as tax filing deadline
  - Contribution deadline for 2024 is 4/15/2025
  - Report contribution on Schedule 1

Retirement Plan Contributions

- Simplified Employee Pension (SEP)
  - Maximum contribution ≈20% of self-employed income or 25% of an employee's earnings
  - Maximum contribution $66,000 in 2023
  - Plan may be established as late as tax filing deadline
  - Contribution deadline is 4/15/2024 or 10/15/24 with extension
  - Cannot discriminate against eligible employees
  - IRS Pub. 560

Retirement Plan Contributions

- Savings Incentive Match Plan for Employees (SIMPLE)
  - Both employee contribution and employer contribution
    - Self-employed individual is both employer and employee
  - Plan must be established by October 1 of prior year
  - Contribution deadline
    - For employee portion, within 30 days of withholding
    - For employer contribution, 4/15/2024 or 10/15/24 with extension
  - Cannot discriminate against eligible employees

Retirement Plan Contributions

- Individual 401(k)
  - Elective deferral of up to $23,000 for 2024 ($30,500 for 50+)
  - Employer portion up to 25% of compensation
  - Individual can make other nonelective contributions
  - Cannot exceed $69,000 for 2024

Health Savings Account (HSA)

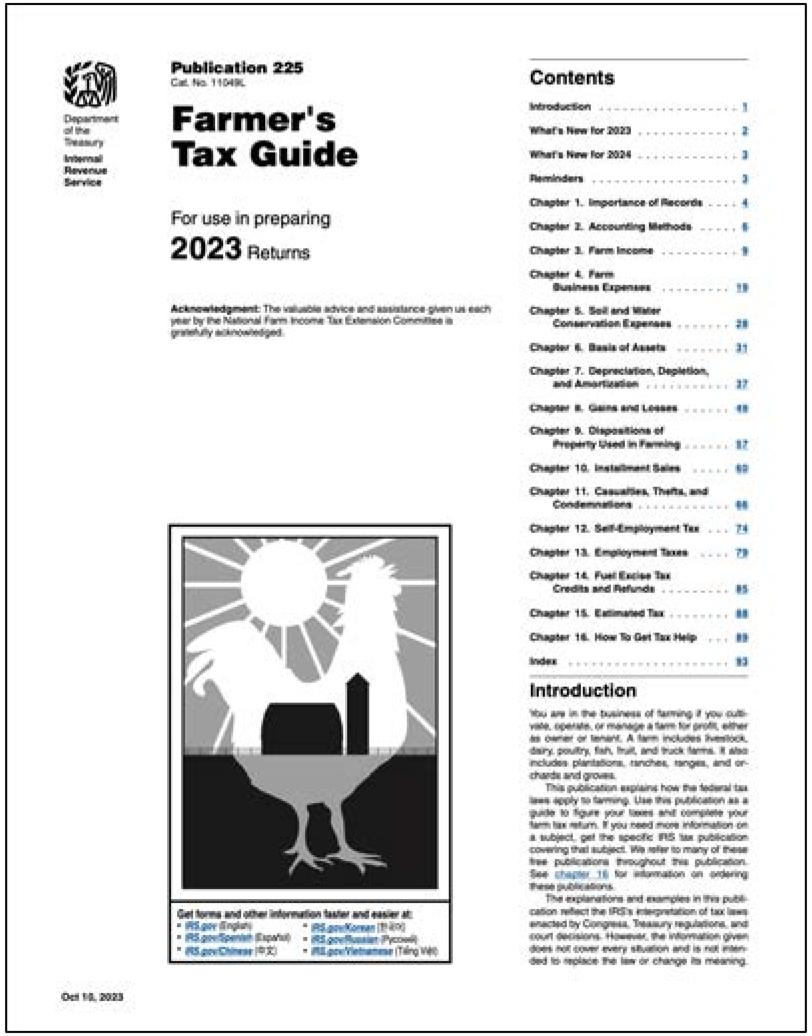
- Must participate in eligible health plan, usually a HDHP
- Contributions are deductible
  - $4,150 for single coverage
  - $8,300 for family
  - Additional $1,000 if 55 and older
  - Contribution deadline is 4/15/2025
- Distributions are tax-free if for qualified medical expenses
- Schedule 1

Tax Planning

- Taxes paid as you go, if no or low withholding, may need to make estimated tax payments during the year
  - Underpayment of estimated tax penalties may apply if late or estimated tax is underpaid
- Qualified farmers not subject to underpayment penalty if:
  - One estimated tax payment is made by January 15, or
  - Income tax return is filed, and all tax paid, by March 1
- Qualified farmer if 2/3 of gross income from farming
- Interactive Tax Assistant (ITA) https://www.irs.gov/help/ita

Resources

- www.IRS.gov
  - Forms
  - Instructions
- Pub. 225 – Farmers Tax Guide
- RuralTax.org
- https://www.farmers.gov/taxes



Department of the Treasury
Internal Revenue Service

Publication 225
Cat. No. 11049L

Farmer's Tax Guide

For use in preparing

2023 Returns

Acknowledgment: The valuable advice and assistance given us each year by the National Farm Income Tax Extension Committee is gratefully acknowledged.

Get forms and other information faster and easier at:
- IRS.gov (English)
- IRS.gov/Spanish (Español)
- IRS.gov/Chinese (中文)
- IRS.gov/Korean (한국어)
- IRS.gov/Russian (Pусский)
- IRS.gov/Vietnamese (Tiếng Việt)

Oct 18, 2023

Contents

Introduction

You are in the business of farming if you cultivate, operate, or manage a farm for profit, either as owner or tenant. A farm includes livestock, dairy, poultry, fish, fruit, and truck farms. It also includes plantations, ranches, ranges, and orchards and groves.

This publication explains how the federal tax laws apply to farming. Use this publication as a guide to figure your taxes and complete your farm tax return. If you need more information on a subject, get the specific IRS tax publication covering that subject. We refer to many of these free publications throughout this publication. See chapter 16 for information on ordering these publications.

The explanations and examples in this publication reflect the IRS's interpretation of tax laws enacted by Congress, Treasury regulations, and court decisions. However, the information given does not cover every situation and is not intended to replace the law or change its meaning.

Thank you for Attending!!

What questions might you have?

For any follow-up questions contact:

janet.wright@usda.gov

Questions