Year-End Tax Planning Tips for Farmers and Cooperatives

Speakers: Paul Neiffer and Rod Mauszycki

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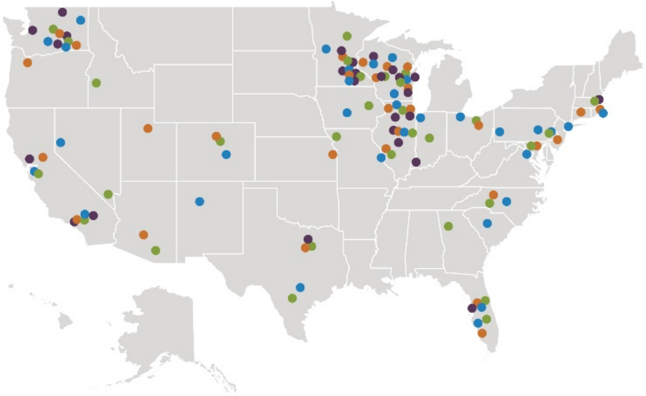

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It Does Not Matter……

December 1, 2019 | by Paul Neiffer

First, I hope everyone had a great Thanksgiving Holiday. I spent the week in San Diego with my family including my only granddaughter who celebrated birthday #1 on Friday. I had a little trepidation in seeing her since the last four times I had visited her in Denver she started crying within 10 seconds of seeing me. However, during this week, she thought her granddad was one of best persons to be around. She even fussed a bit when she saw grandma for the first time but by the end of the week things were back to normal – grandma was #1 and granddad was less than #1.

Now for some tax stuff. We continue to get quite a few comments about how to calculate the Section 199A when dealing with cooperatives. Let's review the history of the old Section 199 deduction. Cooperatives were treated as an "extension" of farmers, therefore, the cooperative would calculate the 9% Domestic Production Activities Deduction (DPAD) on the sales made by the farmer to the cooperative and only the cooperative could receive any DPAD on those sales. The cooperative could then keep it or pass some or all of it to the patrons.

Overview

- We will provide an overview of the following topics:
  - Section 199A
  - Excess Business Limitation
  - Net Operating Loss (NOLs)
  - Accounting Methods
  - Business Interest Expense
  - C Corporations
  - Depreciation
  - Section 1031
  - Charitable Remainder Trust (CRT) and Op Zone

Speaker Introductions

Paul Neiffer is a certified public accountant and business advisor specializing in income taxation, accounting services, and succession planning for farmers and agribusiness processors. Paul is a principal with CLA in Yakima, WA, as well as a regular speaker at national conferences and contributor at agweb.com. Paul regularly publishes timely content on CLA's agribusiness blog, Farm CPA Today.

Rod Mauszycki is a lawyer and principal in CLA's agribusiness and cooperative group, specializing in tax, restructuring and farm transition and succession. Currently he serves as the principal in charge of the agribusiness Midwest region, the principal in charge of producer tax and is co-founder of the agribusiness and cooperatives transition and succession practice.

Section 199A

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199A – General

- Qualified Trade or Business/SSTB
- 20% deduction
- Individuals and partnerships
  - Not C Corps
- Thresholds
  - Single: $160,700 (to $210,700)
  - Married: $321,400 (to $421,400)
- Cooperative DPAD

199A and Self Rentals

- Not all rentals are trade or business
  - Deemed trade or business if common ownership with business
  - Not leased to a C corporation

Rental as Trade or Business

- Continuity and regularity with the intent of making a profit
  - Single property could be a trade or business
  - Delegation of involvement okay
- Cash rental of farm may rise to the level of a trade or business
- Crop share does not necessarily = trade or business

Entity Relationships

Landlord	Tenant	Other Information	Common Ownership
Partnership owned 99% by A, 1% by B	Farm owned 1% by A, 99% by B	A and B and not related.	Yes. The group owns 100% of both. They do not have to each own identical interests.
Partnership owned 99% by A, 1% by B	S corporation farm owned 1% by A, 99% by B	A and B and not related.	Yes. The group owns 100% of both. They do not have to each own identical interests.
Rick	Rick's wholly-owned C corporation		No. Common ownership must be individually or with RPEs. A C corporation is not an RPE.
Julie	Julie's wholly-owned C corporation and 1% by Julie		Should be. The tenant is an RPE. Julie is deemed to own the corporation's stock.
Trust	Trust's 50% beneficiary		Yes, due to Sec. 267(b)(6).
Trust	Partnership between Trust's beneficiary and unrelated individual	Partnership's profit/loss or capital ownership is 50-50.	Yes, due to Sec. 267(b)(6), at 50%.
Individual	Partnership between individual and third party	Partnership's profit/loss or capital ownership is 50-50.	Yes, due to Sec. 707(b)(1).

(p. 1-11)

SSTBs and Agriculture

- Commodities dealing = SSTB
  - Not if physically handling, storing, transporting
- Reputation or skill?
- Partial SSTB taint of entity
  - More than one business
- Common ownership with SSTB taint
  - Not tainted for the non-owner of the SSTB

199A Misc.

- Guaranteed Payment not QBI
  - Preferred allocated ok
- 50% W-2 wage expense
  - Alternatively, 25% of W-2 + 2.5% of UBIA of qualified property
- UBIA at end of year
  - Ten full years or, if longer
  - Last full year of cost recovery

199A Regs

- Released on June 18, 2019
- Allows for any “reasonable” allocation of patron QBI
- Allows for safe harbor method based on revenues
- Grandfathered “three bucket” approach for transition
- Still don’t know:
  - How to allocate Section 1245 gains
  - How to handle negative cooperative QBI
  - Aggregation election of rentals affect on patron QBI

Excess Business Limitation

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Excess Business Loss

- Excess farm loss repealed – need to use excess business loss
- Applied at owner level (taxpayers other than C corps)
- Aggregate all business items
  - $255,000/$510,000
- Excess carried over as Net Operating Loss (NOLs)
- Lots of unknowns

Net Operating Loss (NOLs)

NOLs

- NOL for years beginning after 2017
  - Can’t exceed 80% of pre-NOL income
- NOL for years ending after 2017
  - No carryback except 2 years for farm loss
  - No expiration
  - FIFO

Accounting Methods

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Accrual

- Farm corporations and Partnerships with corporate partners
  - Accrual unless PSC or gross receipts test
- Gross Receipts Test
  - 26 million
  - Not reduced by COGS
  - Reduced by adjusted basis in assets sold
  - Prior three years

Aggregation of Gross Receipts

- Treated as single employer
  - Related parties
  - Affiliated service groups
- Parent-Sub
  - > 50%
  - String
- Brother-Sister
  - Five or fewer persons
    - ◊ At least 80% in each
    - ◊ > 50% considering identical ownership

No Aggregation Example

Example 4 ***No aggregation***

A partnership and a corporation have the following ownership (owners are not related):

	Corn LLC	Wheat, Inc.	Common
Catie	40%	40%	40%
Jack	1%	59%	1%
Grant	59%	1%	1%
	100%	100%	42%

Although the same persons together have a controlling interest (80% or more in each organization), they fail the effective control test (more than 50%, considering identical ownership).

Aggregation Example

Example 5 ***Aggregation required***

Two partnerships have the following ownership (owners are not related):

	Beans LLC	Dairy LLC	Common
Madison	10%	35%	10%
Boe	30%	20%	20%
Troy	25%	20%	20%
Steph	20%	5%	5%
Ted	5%	5%	5%
Other	10%	0%	0%
Other	0%	15%	0%
	100%	100%	60%

The same persons together have a controlling interest (80% or more in each organization). However, we consider up to five owners in the analysis. As a result, Beans top-5 owners with interests in both entities total 90%; the same owners hold 85% of Dairy. The effective control test is also met. Considering identical ownership, the same five individuals have 60% effective control (i.e., more than 50%).

Farm Syndicate

- > 35% losses allocable to limited
  - During any period (rather than during the year)
- Limited don't include
  - Individuals participating in management at least 5 years
  - Individuals living on this farm (no five-year test)
  - Individuals participating in processing livestock from this farm
  - Individuals holding other farming interests
  - Members of family of grandparent of any of the above

Business Interest Expense

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Business Interest Expense

- No limit if gross receipt test met
- Limit at entity level
  - Separate limit at owner level
- Excess carries forward
- Calculation
  - Interest income, PLUS
  - 30% adjusted taxable income, PLUS
  - Floor plan financing interest

Partnership Limitation

- Disallowed at partnership level
  - Nondeductible item to partners
  - Suspended at partner level
  - Reduces basis in partnership interest
  - Adds to basis if partnership interest sold before partner can use
- Deductible when partnership has Excess Taxable Income
- Partner determine ATI without K-1 income
  - Use partnership ETI instead

S Corporations and EBIE

- Same as partnership, except
  - Disallowed at S corporation level
  - Waits for S corporation to have Excess Taxable Income

Opt Out

- Electing farming business
  - Use ADS on 10+ year cost recovery assets
  - Bonus depreciation not available for those assets
  - Use Section 179

C Corporations

C Corporations

- 21% flat rate
- QSBS
  - 5-year holding
  - Originally issued stock
  - C corporation while holding that stock
  - Eligible businesses only (not farming)
- State and local tax deductible
- Section 119 benefit
- S corporation BIG rate = 21%

C Corporation Planning

- Reasonable compensation necessary
- Accumulated earnings tax
- Hold stock until death?

Depreciation

Farm Depreciation

- DDB allowed
- 5-year cost recovery on new farm equipment
- Passenger auto limits increased
- Bonus = 100%
  - New and used
  - Not from a related party
  - Includes Sec. 743(b) adjustments regardless of partnership treatment

Farm Class Lives

- Farmer's Tax Guide
  - New farm equipment = five years
- Land improvements = 15 years
  - Not buildings
- Single purpose ag and hort structures = 10 years
  - Livestock feeding and care, plus greenhouses
- Section 1245 real property = 7 years
  - Look like buildings, but operate as equipment
- Buildings = 20 years

Section 179

- Qualifying assets
  - Equipment
  - Other property used in production or bulk storage of fungible commodities
  - Single purpose ag or hort structure
- $1.02 million for 2019
  - Acquisition limit, start of phase-out = $2.55 million for 2019

Section 179 on Vehicles

- $25,000 Sec. 179 limit on > 6,000 vehicle
- Exceptions that allow full Sec. 179:
  - Seating > 9 persons behind driver (large van)
  - Pickup with ≥ 6 foot box
  - Vans with driver-only seating

Bonus Depreciation Planning

- 20 year property: Shops, machine sheds, residence
- Trade basis counts for bonus
- Conversion to personal use: Recapture prior Sec. 179 if > regular depreciation
  - Bonus depreciation = regular depreciation

Section 179 vs. Bonus

	Sec. 179	Bonus
New vs. used	Both	Both
Trades	Boot only	Entire basis
Effective for	Maximum based upon tax year $1 million, indexed	100% Phases down after 2022
Eligible assets	Sec. 1245 property	Recovery period of ≤ 20 years (i.e., all farm depreciable assets)
Phase-out	Yes, when qualifying property > $2.5 million (indexed)	No

Section 1031

Section 1031

- Real property only
- Personal property exchanges taxable
  - Replacement assets = full basis
  - Section 179 or bonus on replacement?
  - State conformity
- BIG tax implications upon electing S from C

Section 1031

- Real property for real property
  - Real 1245 must be replaced with real 1245
- Recapture potential on sales of property acquired in 1031 exchange
- Exchange of water rights for land

Charitable Remainder Trust (CRT) and Op Zone

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Charitable Remainder Trust (CRT)

- CRT = charitable trust

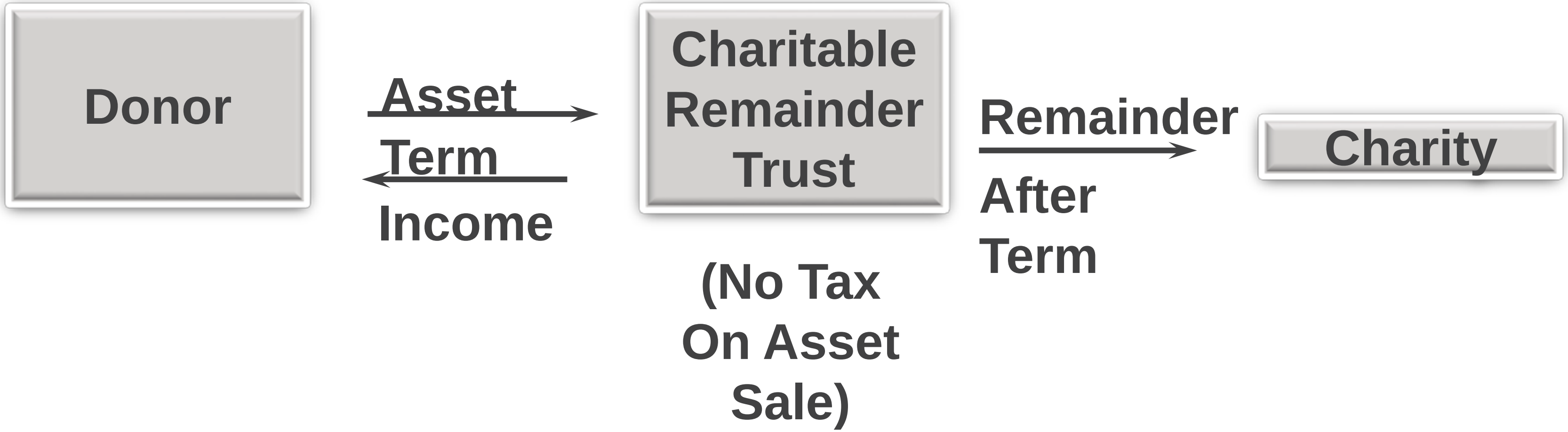
ANNUITY TRUST

- Fixed payout
- No additional funding

UNITRUST

- Payout is % of annual value
- Additional asset input allowed

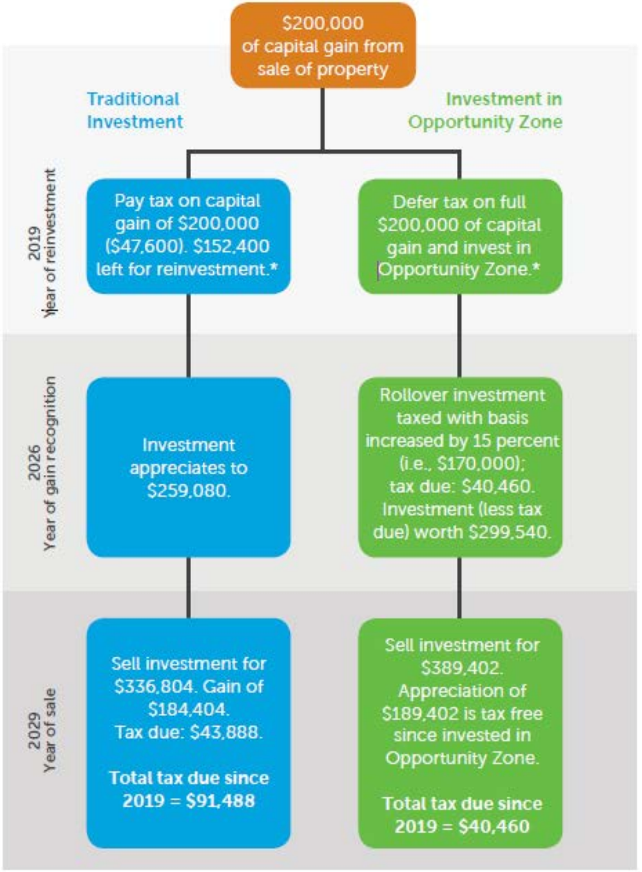
Charitable Remainder Trust (CRT) Chart



Charitable Remainder Trust (CRT)

- Funding a CRT with ordinary farm assets
- No income or SE tax to proprietor on inventory
  - Expenses allowable
  - CRT sells inventory tax-free
  - Distributions from CRT = ordinary income but not SE income

The Opportunity in Opportunity Zones



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