End of Year Considerations and 2020 Tax Planning

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What happened in 2020 that has created this important need for cash basis farmers to seek trusted advice for year-end considerations? Net farm income (a broad measure of profits) in the United States is forecasted to increase 22.7 percent ($19.0 billion) to $102.7 billion in 2020, according to USDA Economic Research Service (ERS) (https://www.ers.usda.gov/topics/farm-economy/farm-sector-income-finances/farm-sector-income-forecast/). If adjusted for inflation, net farm income in 2020 would be 25.4 percent below its peak in 2013 ($137.6 billion), but still 13.8 percent above 2000-2019 average ($90.2 billion).

The projected increase in net farm income is despite forecasted declines of cash receipts (income) for all commodities of 3.3 percent ($12.3 billion) to $358.3 billion in 2020. Higher cash receipts for fruit and nuts is expected to more than offset the loss for corn, soybeans, and wheat. Total animal and product cash receipts are expected to decrease 8.1 percent (14.3 billion) in 2020. Total production expenses are forecasted to decrease 1.3 percent ($4.6 billion) in 2020 to $344.2 billion. Interest expenses and livestock purchases are expected to drop, but fertilizer and cash labor expenses are forecasted to slightly offset this decline.

Government Payments Significantly Increase in 2020

Direct government farm payments – which include Federal farm program payments paid directly to farmers – are expected to be the significant difference in 2020 and are forecasted to increase $14.7 billion (65.7 percent) to $37.2 billion. The anticipated increase is due to supplemental and ad hoc disaster assistance for COVID-19 relief, including payments from the Coronavirus Food Assistance Program (CFAP) ($16 billion) and the Paycheck Protection Program (PPP). Although administered as a "loan," the PPP loans may be forgiven if the program's requirements are met. These loans are treated as a direct payment to farmers by ERS and forecasted at $5.8 billion in 2020. In addition, farmers received Market Facilitation Program (MFP) payments authorized in 2019 but paid in 2020 (3rd round of payments or 25% of total MFP payments). Crop farmers may see payments under the Agriculture Risk Coverage (ARC) program or Price Loss Coverage (PLC) program. The Dairy Margin Coverage Program, which replaced the Dairy Margin Protection Program in the 2018 Farm Bill, is forecast to make net payments of $200 million to U.S. dairy operators in 2020.

Income Bunching

Farmers have experienced a number of challenges in 2020. COVID-19 has caused many ripple effects in the U.S. and among communities in Wisconsin. Unexpected payments may have assisted farmers in weathering 2020 a little better than anticipated. Proper management of this income bunching is important to maximize its benefit when tax planning.

Many of the government program payments must be included in a farmer's gross income in the year that it was received. These payments were issued as a result of a market disruption or price loss and will be taxed as ordinary income. Government program payments are reported on lines 4a and 4b of IRS Form 1040, Schedule F. See Schedule F Instructions, page 4 (https://www.irs.gov/pub/irs-pdf/i1040sf.pdf). In addition, this income will be subject to self-employment tax for farmers. Federal and State government program payments that farmers may have received in 2020 include:

- ARC & PLC program payments (received October or November)
- CFAP-1 and CFAP-2 payments (received June, August, September - December)
- MFP payments (received January or February)
- Wisconsin Farm Support Program (received July or August)

Defer Payments

Farmers may receive crop insurance payments in 2020 as a result of crop damage, drought, freeze, or other crop losses (destruction of crops). In most cases, a farmer must report crop insurance proceeds in the year received. Under some circumstances, the crop payment may be deferred to the following year's income if a farmer typically sells the crop the year following its harvest. Payments from revenue insurance that covers the combination of yield risk (poor crop yields) and price risk (low prices) can be postponed only to the extent they are paid for yield risk.

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