End of Year Considerations and 2020 Tax Planning cont'd

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Also, farmers may have crop and livestock sales that were planned and some that were unexpected. Farmers may want to defer income from commodity sales by utilizing a deferred payment contract and receiving payment the following year. Flexibility is a key feature of these contracts since a farmer may elect to report this income in 2020 or defer the receipts to 2021.

Deferred payment contracts may be done on a contract-by-contract basis with small or large amount of commodity sales over one or multiple contracts. See IRS Farmers (ATG) Chapter Nine – Grain (https://www.irs.gov/pub/irs-utl/farmers_atg_chapter_9.pdf).

Other COVID Relief Payments

Many Americans received their economic impact payment, also called stimulus payment or recovery rebate credit, authorized by the Coronavirus Aid, Relief, and Economic Security Act (CARES Act). These were $1,200 payments ($2,400 for a couple) and $500 for children under 17 years of age. This payment is not income and taxpayers will not owe tax on it. See IRS COVID Tax Tips 2020-55 (https://www.irs.gov/newsroom/what-people-really-want-to-know-about-economic-impact-payments).

A farmer may have received a Paycheck Protection Program (PPP) loan in 2020. As with several government programs during the COVID-19 pandemic, rules and guidance on these programs are always evolving. Current Treasury rules do not allow deductions for expenses paid with forgiven PPP loan proceeds. Current rules indicate forgiven PPP proceeds will not be included in taxpayer's gross income and expenses paid with forgiven proceeds (such as payroll costs) will not be deductible, ultimately avoiding a double tax benefit. Discuss this issue with an accountant or tax preparer for guidance. If a loan hasn't yet been forgiven, the expenses remains deductible. Though the PPP proceeds that are later forgiven could trigger the recovery of these expenses, resulting in income that must be recognized and a future tax liability. If a farm has used all the PPP proceeds even before the 24-week covered period, working on the forgiveness application in tandem with tax preparation may be very helpful for this unprecedented year.

Some farmers also received Economic Injury Disaster Loan (EIDL) advances in the amount of $1,000 per employee (up to maximum of $10,000). These advances (called grants by Small Business Administration) may reduce PPP loan forgiveness. Because the CARES Act does not exclude EIDL grants from gross income (as it does a forgiven PPP loan), these payments should be reported in a farmer's gross income unless additional guidance is provided by IRS.

End of Year Tax Planning

Farmers have several tools available to assist with managing their tax liability, however some of these tools need to be taken advantage of prior to December 31, 2020. Avoiding income spikes and dips prevents overall income from being taxed at unnecessarily high tax rates. Consult with a trusted tax professional to discuss if one of these options may work best for your farm business.

- Prepay farm inputs. Most farmers already understand this but more IRS audit activity on these payments report deposits do not qualify as prepayments. To qualify, prepays should:
  - Have a stated farm input (seed, gas, diesel, fertilizer, chemicals, etc.),
  - Have a stated quantity,
  - Have a stated price per unit,
  - Not allow for a substitution, and
  - Should not exceed 50% of farm expenses (in most situations).
- Income averaging.
- Retirement account contributions.
- Gift commodities to charity.
- Timing purchase or sale of assets.
- Managing deprecation of assets.

Please visit UW Division of Extension's Farm Management website at https://farms.extension.wisc.edu/ for more information.