

Lesson 6.4: Special Tax Rules for Agriculture - Value-Added Inventory

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- through the Food and Ag Impact Project Visit us at <u>https://law.uark.edu/academics/llm-food-ag/</u> •

2

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This presentation is intended to provide general information on agricultural income tax issues and should not be construed as providing legal advice. It should not be cited or relied upon as legal authority. State laws vary and no attempt is made to discuss state specific laws. For advice about how these issues might apply to your individual situation, consult an attorney.

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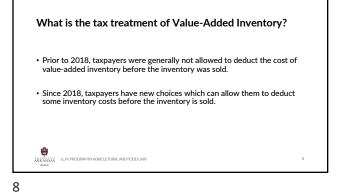




What is Value-Added Inventory?

- For the purpose of this lesson, value added inventory is: items you have physically transformed which you hold available for sale on the last day of your tax year, and which you reasonably expect to sell before the items spoil.
- Note: Growing crops and animals held for sale are not treated as inventory for tax purposes. (All expenses are deducted as they are paid.) See Pub 225 Chapter 3.
- Note: Supplies and inputs on hand at the end of the year are sometimes called "prepaid" and sometimes called "inventory." The tax treatment of supplies and materials used in your farming and ranching operation was covered in Lesson 2. See Also Pub 225 Chapter 4.

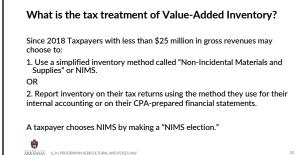
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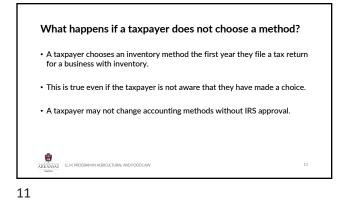
So when can you deduct the costs associated with Value-Added Inventory?

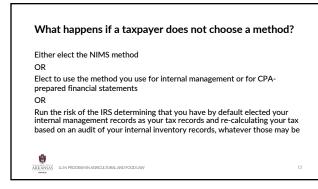
• Generally, you can deduct the cost or an inventory item in the year when the item is sold (not when you incur the expense).

- If you incur the expense and sell the items all in the same year you may choose to do inventory accounting for internal management purposes, but you do not have inventory for tax purposes.
- If you have a cost to create an inventory item in one year, but the item is still on hand at the end of the year and you reasonably expect to sell it in a future year then you need to make a choice about how you will treat the items for tax purposes.



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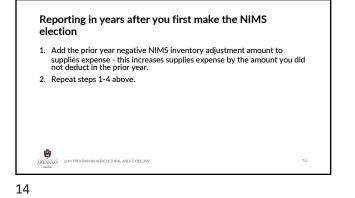


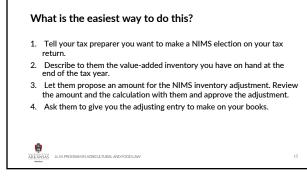




- Determine the direct costs that go into value-added inventory. For NIMS direct costs are supplies and materials you purchased to create or pack the product, or the cost of custom processing/packing.
- 2. Determine how much value-added product associated with those costs is on-hand at the end of the tax-year (generally midnight on 12/31).
- Report Supplies Expense at the full amount on line 28 of Schedule F.
 Add a new expense line called "LESS: NIMS INVENTORY ADJUSTMENT" and record the amount calculated in Step 2 as a "NEGATIVE."

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 A local Small Business Development Center (SBDC) may be able to help you to set up (or clean up and improve) your bookkeeping system and establish methods for tracking inventory.
 The USDA Value Added Producer Grant Program (VAPG) is a costreimbursement program intended to help producers establish profitable value-added businesses. See USDA Rural Development Business Programs.

1IN AGRICULTURAL AND FOOD LAW

16



