



Lesson 6.6: Special Tax Rules for Agriculture - Catastrophe and Disasters



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Legal Disclaimer

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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Program Overview

1. Filing: Federal Income Tax Filing Requirements
2. Records: Recordkeeping Requirements
3. Taxes: Individual Federal Income Tax Return
4. Entities: Business Entities and Federal Tax
5. Agricultural Income: Special Rules
- 6. Special Tax Rules for Agriculture** <- We are here.



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Lesson 6 Overview - Special Tax Rules for Agriculture

- 6.1 USDA Payments
- 6.2 Debt Relief
- 6.3 Mixed Use Real Property
- 6.4 Value-Added Inventory
- 6.5 Conservation
- 6.6 Catastrophe and Disasters** <- We are here.
- 6.6.a Livestock Losses and Weather-Related Sales



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Types of Losses - Causes

This lesson is about the tax treatment of loss of business property and related compensation (from insurance or government programs) due to:

- Theft
- Casualty
- Casualty losses caused by a Federally Declared Disaster

Note that different rules apply for the loss of non-business property such as a personal residence and its furnishings.

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Types of Losses - Property Types - Crops and Livestock Held for Sale

- Most farm/ranch tax returns already deduct all costs associated with producing crops or livestock held for sale.
- Generally, there is no additional deduction associated with this type of loss because all of the costs have already been deducted.
- But, there are some special tax rules to help farmers who have had these types of losses.
- See also Lesson 6.6.a for additional rules for livestock.

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Types of Losses - Property Types - Crops and Livestock Held for Sale

Payments for lost crops or livestock:

- Crop insurance
- Non-insured Crop Disaster Assistance (NAP)
- Other government payments
- Other private income insurance (business interruption insurance)

All of these types of income are taxable, unless Congress has specifically said that a certain type of program payment is not taxable.

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Types of Losses - Property Types - Crops and Livestock Held for Sale

- Payments for lost income are generally taxable.
- A taxpayer may elect not to be taxed on crop insurance or disaster relief payments in the year received, and instead defer the payment to the following year.

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Types of Losses - Property Types - Business Property

- Business property is the assets used in the business including:
- Land improvements including roads, irrigation ponds, planted windbreaks, etc.
 - Buildings, fences, wells, irrigation systems, etc.
 - Tractors, trailers, implements, small tools, etc.
 - Trees, vines and bushes that produce annual crops
 - Livestock not typically held for sale, but used in the business including:
 - Roping horses, working dogs
 - Breeding livestock
 - Dairy animals
 - Laying hens
 - Animals held primarily to produce fiber

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Types of Losses - Property Types - Business Property

- There are a few USDA programs specifically for loss of business property including:
- The Tree Assistance Program
 - The Livestock Indemnity Program

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Tax issues for casualty loss of business property

There are two aspects to taxation for casualty losses of business property:

1. The treatment of the depreciable asset
2. The treatment of any proceeds received from insurance or salvage sale

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The Asset

You will have taxable gain or loss equal to the difference between insurance or salvage sales proceeds and the tax basis of the asset.

To find the tax basis:

1. Identify the asset on the asset list
2. Identify the original cost of the asset
3. Identify the total amount of tax depreciation deductions taken to date - this is called "accumulated depreciation"
4. The difference between 2 and 3 is the "tax basis" of the asset.

Note that the tax basis of an asset is different if the asset was received as a gift or inheritance. See Lesson 2 and Pub 225.

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Tax Loss from Asset Loss

- Tax losses may be claimed in the year experienced.
- Tax losses associated with a federally declared disaster may be claimed in the year PRIOR to the actual loss by amending the prior year return.
- This allows the taxpayer to quickly receive a refund of prior year taxes instead of waiting to report the loss when the tax return is due.

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Tax Loss from Asset Loss

Example:

Purchase Price: \$2,000
Less: Accumulated Depreciation \$1,500
Equals: Tax Basis: \$500

Insurance Proceeds: \$250
Plus: Salvage Sale Proceeds: \$50
Equals: Total Proceeds: \$300

Total Proceeds: \$300
Less: Tax Basis \$500
Equals: Capital Loss (\$-200)

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Tax Gain from Asset Loss

Example:

Purchase Price: \$2,000
Less: Accumulated Depreciation \$2,000
Equals: Tax Basis: \$0

Insurance Proceeds: \$250
Plus: Salvage Sale Proceeds: \$50
Equals: Total Proceeds: \$300

Total Proceeds: \$300
Less: Tax Basis \$0
Equals: Capital Gain \$300

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Tax Gain from Asset Loss and IRC Section 1033

Gain is insurance or sales proceeds in excess of tax basis.
Gain is taxable income.

If the proceeds are used to replace lost property, the gain may be deferred to a future year.

Defer gain by reducing the basis of the new property by the amount of gain. This will:

- o 1. Reduce the depreciation deduction for the new property
- o 2. Increase the gain on the sale of the new property

• Additional considerations include:

- o Deadlines for acquiring new property
- o Allowable types of new property

- Seek additional information regarding **IRC 1033** and the assistance of a qualified tax preparer.

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Clean up and recovery

- Clean up and recovery costs are generally deducted as ordinary and necessary business expenses.
- To the extent that clean up and recovery involves repairing or replacing assets, costs must be capitalized and later deducted through depreciation.

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Questions?
Thank you!

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How do I learn more about federal income taxes and my farm or ranch?

- There are previous lessons in this series.
- For each lesson there is a short set of questions you can answer to help you decide if the training will be useful to you.
- You can access the questions and the trainings here:
- <https://law.uark.edu/academics/llm-food-ag/llm-projects-agftap.php>
- Additional project resources are available here: <https://agftap.org>

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How do I learn more about federal income taxes and my farm or ranch?

IRS Publication 225, The Farmers Tax Guide
RuralTax.org
IRS website and publications

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