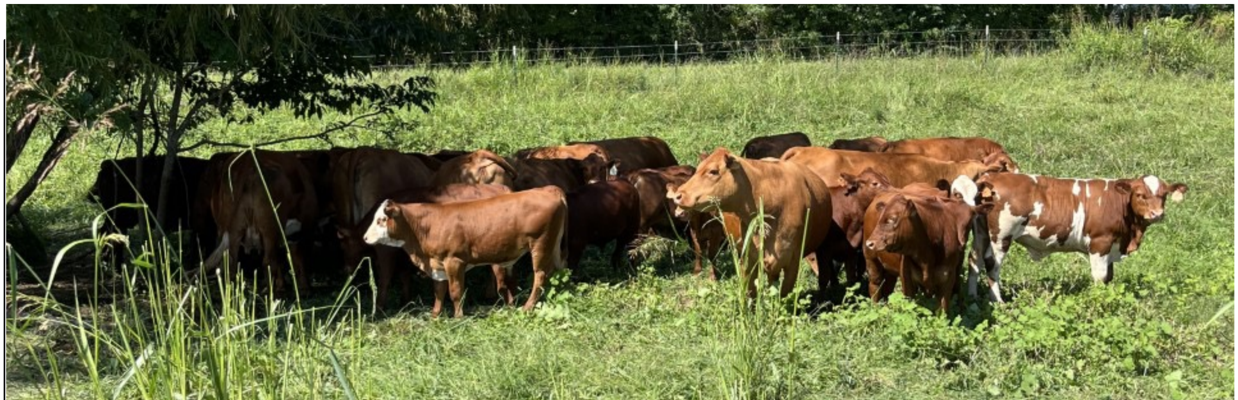

Lesson 6.5: Special Tax Rules for Agriculture - Conservation

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This training provides greater detail on the special tax treatment of conservation expenditures.

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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.

Funding

- This material is based upon work supported by the U.S. Department of Agriculture, under agreement number FSA22CPT0012189.
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This project and materials created by Poppy Davis as part of the LL.M. Program in Agricultural and Food Law at the University of Arkansas School of Law is part of the Agricultural Financial, Tax and Asset Protection program.

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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There were five lessons previously in this series.

The s[illegible]ing covers special tax rules for agriculture.

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 <- We are here.

6.6 Catastrophe and Disasters

6.6.a Livestock Losses and Weather-Related Sales

Annual Conservation Expenditures

- Conservation practices that are part of your normal annual farming practices are usually deducted as ordinary and necessary business expenses.
- Practices that are part of how you:
  - Increase annual soil fertility
  - Manage weeds and pests
  - Improve the quality of your product
  - Provide pasture or forage

For example, if you plant annual cover crops as part of your normal plan for soil fertility that may be considered a conservation practice, and those costs are part of your and necessary farming costs for the year.

Conservation Expenditures for Assets

- Assets which are a key part of your normal farming operation and also a key part of a conservation strategy are treated like any other farm asset.
- Farm Example: You buy or build a hoop house and use it in your normal operations. Capitalize the cost (that means treat the hoop house as an asset) and take a depreciation deduction according to the usual rules for asset depreciation.
- Ranch Example: You cross-fence your property to improve pasture-management. Capitalize the cost (that means treat the fence as an asset) and take a depreciation deduction according to the usual rules for asset depreciation.

Assets which are integral to your ongoing farming or ranching operation and also part of a conservation strategy are treated like any other farm asset and depreciated according to the regular tax rules for depreciating assets.

Using hoop houses and cross-fencing are both recognized by the USDA as conservation practices but there are no special requirements to report them as conservation practices when filing your income tax returns, because the practices are also integral to how you produce crops or livestock.

Conservation Expenditures Not Directly Tied to Production

- A third type of conservation expenditures are those that are not directly related to producing crops or livestock. These include:
  - Soil or water conservation projects such as grading, terracing, planting trees as windbreaks, hedges, or grassed waterways, installing livestock ponds, or fencing off waterways.
  - Projects to create or enhance habitat, especially for rare, threatened or endangered species.

These practices are designed to protect soil and water, prevent erosion and protect certain endangered species. So even though they are not part of annual production prac[illegible]y may ultimately improve the productive capacity of the land.

Deducting Conservation Expenditures Not Directly Tied to Production

Taxpayers may elect to deduct as long as:

1. The land is used and was previously used in the business of farming or ranching.
2. Expenditures are to implement a plan approved by the USDA Natural Resources Conservation Service

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Taxpayers may elect to deduct conservation costs not directly tied to production as long as:

1. Th the business of farming or ranching
2. The land was previously used for farming or ranching (so not land recently brought into production)
3. The conservation expenditures are to implement a conservation plan approved by the USDA Natural Resources Conservation Service

Deducting Conservation Expenditures Not Directly Tied to Production

- The deduction for each year is limited to 25% of gross income from farming and ranching for that year.
- Excess may be carried forward for future tax years until fully deducted.

Gross income from farming and ranching in this case includes gains from sales of breeding or dairy livestock or draft animals.

NRCS Payments to Cover Implementation Costs

See Lesson 6.1 for the tax treatment of the income from EQIP.

Expenditures to complete an EQIP-funded project are treated as discussed above:

1. As ordinary and necessary business expenses
2. As purchase costs for assets used in the ordinary course of business
3. As land improvements subject to deduction limitations (for conservation projects not directly tied to annual production practices).

If you participate in the NRCS EQIP program, you will receive income to compensate you for the cost of implementing an approved conservation practice.

The income will be reported to you and the IRS on a Form 1099-G.

Report the income on your Schedule F. You may be able to exclude a portion of the payment if you meet certain conditions. See Cost-Sharing Exclusion section of Publication 225, Farmer's Tax Guide.

Be sure to deduct all the associated expenses according to the rules for ordinary and necessary business expenses, assets, and deducting conservation expenses not directly tied to production.

Other Conservation Payments

- USDA also makes other payments related to conservation practices. See Lesson 6.1 for a discussion of the tax treatment of those payments.

Questions?

Thank you!

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

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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