Planning Considerations for Ranchers and Farmers
under the 2017 Tax Cuts and Jobs Act*

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Taxpayers who operate farms and ranches in the U.S. could realize significant benefits from changes to the tax laws as a result of the passage of the "Tax Cuts and Jobs Act" late last year.

Below is a summary of some changes in the law as well as how the new rules may be utilized to the benefit of farmers and ranchers:

By Jeff Carson

Net Operating Losses (NOL):

- These can now be carried forward indefinitely. Under prior law, they could only be carried forward 20 years.
- NOL deductions are limited to 80 percent of taxable income.
- They can be carried back for two years for farm and ranch businesses. Under prior law, NOLs could be carried back five years.

Qualified Business Income Deduction (QBID):

- For tax years beginning after Dec. 31, 2017, taxpayers (other than corporations) may be entitled to a deduction of up to 20 percent of their qualified business income from a qualified trade or business (including income from a pass-through entity, but not from a C corporation) plus 20 percent of qualified real estate investment trust dividends and qualified publicly traded partnership income.
- The deduction is subject to multiple limitations such as the type of trade or business, the taxpayer's taxable income, the amount of W-2 wages paid with respect to the trade or business, and the unadjusted basis immediately after acquisition of qualified property held by the trade or business.
- The deduction can be taken in addition to the standard or itemized deductions. In some cases, patrons of horticultural or agricultural cooperatives may be required to reduce their deduction. (The IRS will be issuing forthcoming separate guidance for co-ops.)

NOTE: For a more in depth discussion of the complex rules involving the QBID, see the Diversified Trust whitepaper, "The New Section 199A Deduction for Qualified Business Income" by Kim D. Garcia

Accounting Method Changes:

- Under the new law, more farm corporations and partnerships can use the cash basis of accounting for tax purposes. This includes small business taxpayers such as farmers and ranchers with average annual gross receipts of $25 million or less in the prior three-year period.

* Adapted from IRS "Tax Tips" 2018-169 & 2018-170

Depreciation:

The Tax Cuts and Jobs Act made changes to how farmers and ranchers may depreciate farming business property.

Depreciation is an annual income tax deduction. It allows a taxpayer to recover the cost of certain property over the time that they use it. When figuring depreciation, taxpayers consider wear and tear, and deterioration of the property, as well as whether it's now obsolete.

Below is some information about how the tax law changes to depreciation may affect the bottom line of a rancher or farmer:

- New farming equipment and machinery is now classified as "five-year" property, which means that for property placed in service after Dec. 31, 2017, the recovery period is shortened from seven to five years for machinery and equipment.
- The shorter recovery period does not apply to:
  - grain bins
  - cotton ginning equipment
  - fences and other land improvements
- Used equipment remains "seven-year" property.
- Property used in a farming business and placed in service after Dec. 31, 2017, is not required to use the 150 percent declining balance method.
  - Farmers and ranchers must continue to use the 150 percent declining balance method for property that is 15 or 20 years old to which the straight-line method does not apply and for property that the taxpayer elects.
- New and certain used equipment acquired and placed in service after September 27, 2017, qualifies for 100 percent first-year bonus depreciation for the tax year in which the property is placed in service.
- A taxpayer may elect to expense the cost of any Section 179 property and deduct it in the year the property is placed in service.
  - The new law increased the maximum deduction from $500,000 to $1 million.
  - It also increased the phase-out threshold from $2 million to $2.5 million. Adjusted for inflation, for taxable years beginning after 2018.
- The new law increases the bonus depreciation percentage from 50 percent to 100 percent for qualified property acquired and placed in service after Sept. 27, 2017.
  - The bonus depreciation percentage for qualified property that a taxpayer acquired and placed in service before Sept. 28, 2017 remains at 50 percent.
  - Special rules apply for longer production period property and certain aircraft.
- The definition of property eligible for 100 percent bonus depreciation was expanded to include used qualified property acquired and placed in service after Sept. 27, 2017 (if several factors are met).
- Farming businesses that elect out of the interest deduction limit must use the alternative depreciation system to depreciate any property with a recovery period of 10 years or more.
  - Property such as single purpose agricultural or horticultural structures, trees or vines bearing fruit or nuts, farm buildings and certain land improvements.

ATLANTA
877.955.8266

CHARLESTON
866.619.1003

GREENSBORO
855.821.4999

MEMPHIS
800.264.7498

NASHVILLE
877.386.7332

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