

Budget deal delivers tax relief

New tax bill allows expanded deductions for many aspects of a farm business.



At the end of 2010, taxpayers in the United States were eager for leaders in Washington to create and pass a tax bill. The outcome was surprising: Congress passed (with large bipartisan support) an extension of the Bush-era tax cuts, then provided some new tax cuts for 2011 and 2012.

Here are some of the ramifications of this new legislation:

Bonus depreciation

There's still time in 2011 to build that general-purpose machine shed. Bonus depreciation is now 100 percent of the purchase price for certain qualified property that is placed in service before Jan. 1, 2012. This means you can deduct the entire cost of the asset in the first year of ownership.

Believe it or not, there's no dollar limit. Both smaller and larger farms can take advantage. You can claim

100 percent bonus depreciation that will create a loss for your operation. For 2012, the 100 percent bonus depreciation is scheduled to be replaced by 50 percent bonus depreciation. That's still good, but not as good as 2011's level of 100 percent.

Please consult your tax/financial adviser for assistance in determining if the assets you've purchased qualify for this tax deduction. You also need to determine if taking advantage of this part of the tax code fits into the long-term management of your operation. (Note: Your state's department of revenue may handle bonus depreciation differently than the IRS. Find out if there are any differences.)

To be eligible for 100 percent bonus depreciation deduction, an asset must pass these three tests:

1. It must be qualified property. This could include buildings or equipment with a life of no longer than 20 years.
2. It must be purchased and put to use by Dec. 31, 2011.
3. It must be new (rather than used).

179 Expense Election rises

The Small Business Jobs Act also increased the IRS Code Section 179 Expense Election to a maximum of \$500,000 for 2010 and 2011 for qualifying assets. You're now able to deduct the entire cost — up to \$500,000 — of assets in the first year of ownership.

Even better, the Section 179 deduction is available for both new and used equipment. If you've already used the item, the Section 179 deduction isn't available to you. The maximum deduction phases out dollar-for-dollar once a business's eligible asset purchases exceed \$2 million. You can't claim Section 179 deductions that will create a loss. For tax year 2012, the maximum Section 179 deduction is scheduled to drop back to \$125,000 with the

deduction phased out when eligible asset purchases exceed \$500,000.

If you're financing your capital purchases, be careful about using the Section 179 Expense Election. You may put yourself into a situation where you have fully recovered the cost of the asset, but you still have multiple years of payments to make. This applies to the bonus depreciation noted above. Please consult with your tax/financial adviser for help determining whether your purchased assets qualify for these deductions and whether they make sense for your business.

Capital gains relief

Very favorable capital gains rates remain in play. Long-term capital gains rates continue to be 0 percent for taxpayers in the two lower tax brackets (the 10 and 15 percent brackets) established by the IRS. If you're in the 25 percent bracket or higher, the tax rate on long-term capital gains is 15 percent — still a very low tax rate.

These favorable long-term capital gains rates are set to expire at the end of 2012. It remains to be seen whether they'll extend beyond that date. That's up to our legislators and makes planning difficult.

Short-term capital gains continue to be taxed at rates based on the bracket you are in. Consult with your tax adviser if you have assets with a large amount of long-term capital gains and try to time the date of sale to your best advantage.

Lower payroll taxes

If you use hired labor on your operation, you should be aware Congress has reduced the employee's share of payroll Social Security taxes by 2 percent (from 7.65 to 5.65 percent) for a year.

The taxable wage base for the Social Security tax is \$106,800 — allowing a

maximum savings of \$2,136 per worker. The employer sees no reduction in his or her share of the Social Security tax. Again, ask your tax adviser if you have questions about how to get this done correctly.

A lower energy credit


Residential energy efficiency credits are not quite as generous as in the past. For 2011, the credit is only 10 percent of the cost of your qualified improvements, with a maximum credit of \$500.

Requirements in 2011 are more strict than they were in 2010. You have to make sure property qualifies to receive this credit. If you've taken a full or partial credit in a prior year, you may only be eligible for a partial credit. Some improvements that qualified in the past may not be eligible for any credit.

For 2011, high incomes no longer limit a taxpayer from converting a traditional IRA to a Roth IRA. But the 2010 tax law that permitted these conversions and extended the tax liability over a two-year period is no longer in effect.

Machinery considerations

This isn't new, but it could affect you if you're considering the purchase of new machinery that qualifies for either 100 percent bonus depreciation or the Section 179 Expense Election. Rather than trading in your current item for a new asset, consider selling the old one and paying cash for the negotiated price of the new asset.

Doing this ensures you pay income tax on any gain on the sale of the current item, but it may permit a larger bonus deduction or Section 179 Expense Election. The larger deduction is allowed because you can take this deduction on the Schedule F form, which allows a deduction for both self-employment taxes and income taxes. 



Editor's note: Kent Vickre and Dwight Raab write a tax and finance column for each issue of Pioneer GrowingPoint® magazine. Vickre is state coordinator of the Iowa Farm Business Association. Raab is state coordinator of Illinois Farm Business Farm Management. They address issues that influence agribusiness success.

