

# DTN Ag Summit 2012

## Agriculture's Taxmageddon

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# Understanding the “Cliff”

## Key Tax Components:

- **2012 AMT patch and 2012 extenders**
- **2013 income tax increases**
  - Including 2013 estate and gift system
- **Expiring economic stimulus provisions**
- **The 2013 rate increases from Affordable Care Act**
  - 3.8% net investment income tax
  - 0.9% high earner Medicare surtax
- **Strategies**

# The 2012 Extenders

- **AMT patch: Bi-annual adj. of AMT exemption to keep AMT system in sync with regular tax indexing**
  - No patch: All joint TRs > \$60K in AMT!
- **Other key extenders (about 30 in total):**
  - Research tax credit
  - Work Oppty. tax credit (jobs credits)
  - State sales tax deduction
  - Tuition deduction
  - Teacher supply deduction
  - IRA to charity for post-age-70½
  - Etc., etc.

# The 2012 Extenders

- **Expect all to be enacted in December**
- **But delayed 2012 tax filing season**
  - **IRS e-filing and refund delays**

# The 2013 Tax Rate Cliff

- **Expiration of 2001/2003 tax rate system at 12-31-2012:**
  - Higher income tax rates at all brackets
  - Compression of brackets
  - Higher capital gain and dividend rates
  - Marriage penalty (lower jt. std. ded. vs. single status)
  - Phase-outs of itemized and exemptions for higher earners
  - Lower child tax credit (\$1,000 to \$500)

# 2013 Tax Rate Increases

<u>Taxable Income-Jt.</u>	<u>2012</u>	<u>2013</u>
\$ 0 - \$ 17K	10%	15%
\$ 17K - \$ 71K	15%	15%/28%
\$ 71K - \$143K	25%	28%
\$143K - \$217K	28%	31%
\$217K - \$388K	33%	36%
> \$388K	35%	39.6%

# Dividend and LTCG Rates

	<u>2012</u>	<u>2013(?)</u>
<b>Dividends</b>		
– Low brackets	0%	15%
– Upper brackets	15%	28%-39.6%
<b>LTCG</b>		
– Low brackets	0%	10%
– Upper brackets	15%	20%
– > 5 yr. holding per.		18%
<b>Net Investment Income tax</b>	–	3.8%

# 2013 Income Tax Rate Issues

- **Bottom line: Significant tax increases for all taxpayers (and lower rebates for nonpayers)**
- **Result: Compromise likely, but late December**
  - Neither side has total control
  - Fragile economy
  - **2013 tax rate system, if unchanged, adverse to ALL filers**

# The Tax Rate Cliff Tensions

- **Administration:**
  - Rates to 36% - 39.6% on incomes > \$200K/\$250K
  - 20% LTCG rate and increased dividend rate on incomes > \$200K
- **Republican House:**
  - OK with tax increases affecting upper incomes, but not via increases to two top rates (use deduction caps, rates on other income, phase-outs, etc.)

# 2013 Estate and Gift Tax Cliff

	<u>2012</u>	<u>2013</u>
• Estate-gift exemption	\$5.12M	\$1.0M
• Top rate on excess	35%	55%
• History lesson:		
– 2009: \$3.5M and 45% on excess (= Obama's proposal for 2013)		

# Expiration of Economic Stimulus Provisions

- **Business incentives**
  - **100%/50% bonus depreciation (new only;  $\leq 20$  yr. recov.)**
  - **Expanded Sec. 179 deduction (new and used)**
- **Individuals: 2% payroll tax cut**

# Bonus Depreciation

<u>Placed in Service</u>	<u>First Yr. %</u>
Jan. 1, 2008 – Sept. 8, 2010	50%
Sept. 9, 2010 – Dec. 31, 2011	100%
Jan. 1, 2012 – Dec. 31, 2012	50%
Jan. 1, 2013 →	0%

# Section 179 Provisions

<u>Tax yr. beginning in</u>	<u>Sec. 179 Limit</u>	<u>Asset Addn. Phase-out Range</u>
2007	\$125,000	\$500K - \$625K
2008-09	\$250,000	\$800K - \$1.25M
2010-11	\$500,000	\$2M - \$2.5M
2012	\$139,000	\$560K - \$699K

- 2012 amounts = pre-recession 2007 plus indexing
- 2013: ?? (Reverts to old \$25K limit)

# Example: Declining Depreciation Incentives

## Farm machinery:

Active farmer

	<u>2011</u>	<u>2012</u>	<u>2013</u>
Cost – New assets	\$739,000	\$739,000	\$739,000
- Sec. 179	-	(139,000)	(139,000)
- 100%/50% bonus	<u>(739,000)</u>	<u>(300,000)</u>	<u>-</u>
Balance (for regular depr.)	<u>\$ - 0 -</u>	<u>\$300,000</u>	<u>\$600,000</u>

# Expiration of Stimulus Provisions

- **Extension of 2011-12 payroll tax cut of 2%: Probable**
- **Extension of business depreciation incentives: Less likely**

# 2013: New Taxes under ACA

- **3.8% Net Investment Income tax**
  - Interest, dividends, annuities, royalties, rents (without ability to group rental and business to avoid rent status)
  - Passive business income (under 500 hrs. participation)
  - Trading in financial instruments/commodities
  - Net gains, other than from property in a material participation business and entity sale of MP partnership or S corp.
- **Applies to lesser of NII or AGI > \$250K jt./\$200K sgl.**

# Calculating the 3.8% Tax on NII

- Example (Single filer)

## 3.8% Tax

S corp.: farm \$180,000

Rent – net 80,000

AGI \$260,000

– Threshold (200,000)

NII \$80,000

Excess AGI 60,000 Smaller  
x 3.8%

\$ 2,280

# 2013: New Taxes under ACA

## In the bullseye for the 3.8%:

- **Business income from passive entities**
  - Consider grouping election with other active entities
- **Rental net income**
- **Capital gains from all sources except MP pass-thru business**
- **Estates and trusts w/ undistributed taxable income**
  - Applies to retained income > \$12K

# 2013: New Taxes under ACA

## 0.9% Medicare Surtax

- Applies to wages and SE income
- Annual amount > \$200K single or \$250K joint
  - Employer withholds >\$200K; the 1040 adjusts final tax for additional SE income or joint computation >\$250K

# Last Minute 2012 Tax Strategies if Rates Up

**And if income/gain recognition is imminent 2013 & ff.**

- **Accelerate compensation or Schedule F income**
  - Avoid 0.9% plus any ordinary rate increases
- **Sell and repurchase appreciated stock**
  - Avoid 3.8% plus any capital gain rate increase
- **Pay a dividend from closely-held C corp. (if gain on sale/liquidation/redemption is imminent)**
- **Partially redeem a shareholder who might sell soon**
  - May be recharacterized as a 15% dividend

# Last Minute 2012 Tax Strategies if Rates Up

- **Elect out of installment sale treatment on 2012 sale**
- **Trigger a disposition of pre-2012 installment sale receivable to accelerate gain (e.g. gift to kids)**
- **At preparation of 2012 tax return, elect out of deferred gain sale treatment on selected contracts**

# Farm Tax Planning

- **Crop insurance deferral election**
  - All or none
  - Eligible if >50% of crop normally deferred
- **Deferred grain sales: Can elect to tax in yr. sold**
- **Prepaid expenses: OK if actual purchase, not deposit**
  - Invoice for specific goods, specific price

# Tax Strategies

- **Thanks for attending!**
- **Questions??**