

## Weather-Related Sales of Livestock

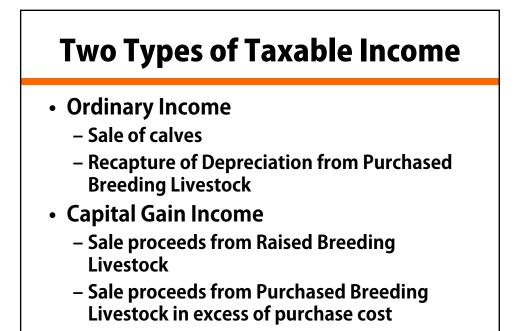
- Applies to sales of livestock due to weather-related conditions: flood, drought, or other weather-related condition causing a shortage of water and/or feed.
- Allows taxpayer to postpone recognition of income from the sale proceeds (to avoid bunching of income).

## Sources for Drought and Disaster Information

- FEMA Presidential declarations
- Farm Service Agency (FSA) Secretary of Agriculture declarations
- U. S. Drought Monitor State and National drought intensity maps refer to <u>http://droughtmonitor.unl.edu/</u>



- Both tax treatments or rules apply to sales in excess of usual or normal due to weather-related conditions.
- The first applies to sales of any livestock (IRC § 451(e) Deferral of Income for 1 Year).
- The second applies to sales of livestock (other than poultry) held for draft, breeding, or dairy purposes (IRC § 1033(e) Involuntary Conversion).



## 1. Deferral of Income for 1

**Year IRC** §451(e)

- The drought, flood, or other weather-related condition must be of such severity that an area affecting the taxpayer's area is designated as eligible for Federal disaster assistance.
- A taxpayer needs to show that the weatherrelated condition caused the sale of more animals than normal.
- Farmer (taxpayer) must use the cash method of accounting.

### **1. Deferral of Income for 1 Year** IRC §451(e)

- Applies to any livestock (including draft, breeding, or dairy animals) sold due to weather-related conditions.
- Sale proceeds (income) may be deferred to the next taxable year, however certain requirements must be met.

### 1. Deferral of Income for 1 Year IRC §451(e)

Requirements that the taxpayer must meet:

- 1. Principal business must be farming (50% of gross income must come from farm business).
- 2. Must use the cash method of accounting.
- 3. Must show that the animals would normally have been sold in the following year.
- 4. The weather related condition that caused the area to be declared eligible for Federal assistance must have caused the sale.

#### **1. Deferral of Income for 1 Year** IRC §451(e)

 The livestock <u>do not</u> have to be raised or sold in the declared disaster area, but the weather-related condition that caused an area to be declared eligible for federal assistance must have caused the premature sale of the livestock.

### 1. Deferral of Income for 1 Year IRC §451(e)

- The sale can take place <u>before</u> or <u>after</u> an area is declared eligible for federal assistance as long as the same weather-related condition caused the sale.
- Taxpayer's history is used to determine the number of animals that would have normally been sold compared to those sold prematurely.

### **1. Deferral of Income for 1 Year** IRC §451(e)

- The sale proceeds from those animals that were sold prematurely, can be deferred and reported as income in the year following the year of the sale.
- Attach a statement to tax return showing normal and excess sales and evidence of the weather-related conditions causing the county to be declared a Federal disaster area.

#### 2. Involuntary Conversion IRC §1033(e)

- Must plan to purchase replacement draft, breeding, or dairy livestock within a 2 year period. (This rule does not apply to poultry or calves.)
- Replacement period can be extended from 2 years to 4 years if the area has been declared eligible for disaster assistance by the Federal government or by one of its agencies.
- If drought persists for more than 3 years, the replacement period can be longer.

### 2. Involuntary Conversion IRC §1033(e)

- Livestock (draft, breeding, or dairy) held for any length of time and a weather-related condition caused the sale.
- Gain realized from the sale can be postponed if the sale proceeds are used to purchase replacement livestock within the time period previously described.
- Replacement animals must be used for the same purpose as those sold. (dairy for dairy and breeding for breeding)

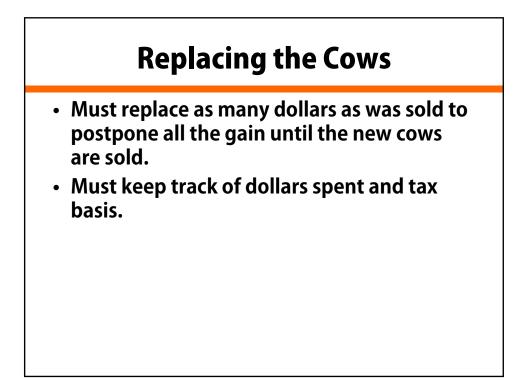
#### 2. Involuntary Conversion IRC §1033(e)

- There is no requirement that the weather-related conditions cause the area to be declared a disaster area by the Federal government for the involuntary conversion rules to apply.
- A taxpayer needs to show that the weather-related conditions caused the sale of more animals than normal.

### 2. Involuntary Conversion IRC §1033(e)

To make the election to defer, attach a statement to the tax return showing:

- Evidence of the weather-related condition.
- Computation of the amount of gain realized.
- Number and kind of livestock sold.
- Number and kind of livestock that would have been sold under usual or normal business practices.



# **Which Option to Select**

- Not an easy answer.
- Everyone's economic situation, tax situation, and goals will be different.
- Consider the following points!

# Points to Consider (cont)

- Future income tax rates
  - 2012 = 10, 15, 25, 28, 33, and 35%
  - 2013 (projected) = 15, 28, 31, 36, and 39.6%
- Future capital gain rates
  - -2012 = 0 or 15%
  - 2013 (projected) = 10% or 20%

## Change in Economic Circumstances: Now What?

• If is not feasible to reinvest proceeds in replacement livestock, producer can invest in similar or related in business use property including real property

## **Which Method to Select?**

Refer to RuralTax.org and Tax Topics: Weather-Related Sales of Livestock Take the information to your tax preparer and have them evaluate the tax consequences of each alternative. (1033(e) Involuntary Conversion vs. 451(e) Deferral of Income for 1 Year) Everyone's situation will be different!!!

## **Contact Information**

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