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CARES Act Implications on Tax Planning for Farmers

The CARES Act, passed in March of 2020, provided many changes that directly impacted farmers. It created both the Payroll Protection Program (PPP) and Economic Injury Disaster Loans (EIDL), which many farmers utilized. However, the CARES Act included several other provisions that didn't get as much attention. Farmers need to be aware of these as they go into tax planning this fall, as they could benefit their operations.

Net Operating Losses

The Tax Cuts and Jobs Act (TCJA) limited some choices we had when it came to Net Operating Losses (NOLs). Prior to 2018, most businesses could carry a loss back for two years, while farmers could go back 5 years. The Tax Cuts and Jobs Act eliminated the ability for non-farm businesses to carry losses back and limited farm loss carrybacks to 2 years and reduced the farm carryback from 5 years to 2 years. The CARES Act delayed the impact of the Tax Cuts and Jobs act until after December 31st, 2020.

In simpler terms, if you had net operating losses in 2018 or 2019, you may want to carry the loss back if you paid taxes in 2013-2017. The decision will be based on if the level of tax was higher in those years than in the future years. The tax brackets in those years were higher than what we expect to see in 2021 – 2025 due to the changes in the TCJA, but that is all subject to future tax law changes as well. The other benefit to carrying the loss back is the time value of the money. Having the refund in your hands now will increase cash flow and working capital rather than waiting for the benefit in future tax years.

This is obviously a complex issue that can be confusing with all the law changes we've been experiencing. If you had losses in 2018 or 2019, you need to discuss the pros and cons of both carrying the loss back and electing to carry it forward on your 2020 return.

Business Losses

A Net Operating Loss occurs when your business losses exceed your non-farm income, which results in negative total income on your return. The TCJA put a limit on business losses of $250,000 ($500,000 for Married Filing Jointly). Any loss greater than this limit is considered to be an Excess Business Loss. This means that if you are married filing jointly and your Schedule F was more negative than $500,000, the loss was limited. The CARES act suspends this rule for 2018-2020.

As a result, if your 2018 or 2019 return was affected by an Excess Business Loss, it will need to be amended. Even though it was prepared correctly at the time, the law is no longer in effect. This

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could change how much of an NOL you generate or could allow you to offset larger amounts of non-farm income.

Required Minimum Distributions

The CARES act suspended the requirement for individuals to take a required minimum distribution (RMD) from their retirement accounts. An RMD is usually required by an individual who is over the age of 70 ½ who has a tax deferred retirement account. The ability to not take a distribution allows for your savings to grow and reduce your taxable income for 2020.

As a side note, the SECURE Act of 2019 increased the RMD age to 72 starting in 2020, so if you turned 70 ½ in 2020, you will not be required to take an RMD until you turn 72.

Retirement Account Changes

The CARES act allows for individuals to take a qualified distribution (up to $100,000) that would not be subject to the 10% penalty for early withdrawals. The individual can also spread the income equally over three years to lower the tax implication of the withdrawal. If the money is replaced within three years, it can be treated as if it was a qualified rollover and the tax will not be due.

This provision may allow you to increase some working capital and cash flow for the next few years, but it's important to remember that if you plan on replacing it, you will have to generate cash flow from another area to avoid the tax.

Charitable Donations

One final change to be aware of is an above the line deduction for charitable donations up to $300. This means you can deduct up to $300 of cash donations without itemizing your deductions. You still need a receipt from the charity to prove the deduction, but if you've gotten out of the habit of keeping those receipts, you should begin keeping at least $300 worth of these receipts.

If you are in the market to make a large donation, they also changed the limit for 2020. In 2020 only, you will be allowed to deduct up to 100% of your adjusted gross income as a charitable donation (you must itemize in this case). Normally, the limit is 60% of your adjusted gross income, so if you were thinking of making a sizable donation, this is the year to do it.

There are many things that have changed this year, but the importance of tax planning is not one of them. There are constantly changing rules, incentives, and pitfalls. It is important to seek the advice of a tax professional to know and understand how each of these things will affect your operation.