TEACHING MANUAL

FARM INCOME TAX MANAGEMENT AND TAX REPORTING

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<table>
<thead>
<tr>
<th>Topic</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Farmer's Tax Calendar for 1970</td>
<td>1</td>
</tr>
<tr>
<td>Tax Forms Needed by New York Farmers</td>
<td>2</td>
</tr>
<tr>
<td>Tax Reform and Farm Tax Reporting</td>
<td>3</td>
</tr>
<tr>
<td>Investment Tax Credit</td>
<td>5</td>
</tr>
<tr>
<td>Depreciation</td>
<td>9</td>
</tr>
<tr>
<td>Guidelines for Depreciation for Farm Assets</td>
<td>11</td>
</tr>
<tr>
<td>Capital Gains and Losses</td>
<td>12</td>
</tr>
<tr>
<td>Tax Savings in Trading Farm Property</td>
<td>15</td>
</tr>
<tr>
<td>Income From Wood, Timber and Christmas Tree Sales</td>
<td>17</td>
</tr>
<tr>
<td>Land Clearing Expense</td>
<td>18</td>
</tr>
<tr>
<td>Farm Partnerships</td>
<td>18</td>
</tr>
<tr>
<td>Tax Considerations in Incorporation of the Farm Business</td>
<td>19</td>
</tr>
<tr>
<td>Social Security</td>
<td>24</td>
</tr>
<tr>
<td>Employees' Social Security and Income Taxes</td>
<td>26</td>
</tr>
<tr>
<td>The Retirement Income Credit and Farmers</td>
<td>27</td>
</tr>
<tr>
<td>Retirement Plans and Income Tax Management</td>
<td>30</td>
</tr>
<tr>
<td>Federal Income Tax Suggestions for Part-time Farmers and Country Dwellers</td>
<td>32</td>
</tr>
<tr>
<td>New York State Investment Credit</td>
<td>34</td>
</tr>
<tr>
<td>The New York State Personal Income Tax</td>
<td>35</td>
</tr>
<tr>
<td>The New York State Unincorporated Business Tax</td>
<td>39</td>
</tr>
<tr>
<td>Farm Tax Tips</td>
<td>40</td>
</tr>
</tbody>
</table>
FARMER'S TAX CALENDAR FOR 1970

There have been no changes in important tax dates for 1970. Important dates for New York farmers to keep in mind in regard to tax obligations are as follows:

**January 15** - Deadline for farmers who elect to file an estimate of Federal income tax due. Farmers may also elect to file an estimate of New York State income tax due on this date. When these estimates are used, the corresponding final Federal and/or State returns are due April 15.

**January 31** - Deadline for a farmer to file Federal income tax Forms W-2 and W-3 if at least one individual was paid $600 or more. If optional Form W-2 is used copies 1 and 2 take the place of State Form IT2102.1

- Deadline for filing Form 943. This year-end Social Security report on hired help must be filed by any employer who paid on employee $150 or more cash wages during the year for agricultural labor, or who had an employee who performed agricultural labor on 20 or more days for cash wages on time basis. An employer who has made monthly deposits sufficient to cover his full tax liability is allowed 10 days additional for filing year-end report.

**February 15** - Deadline for filing Federal and State income tax returns and New York State unincorporated business tax, unless the farmer elected to file estimates on January 15.

**February 28** - Deadline for filing New York State Form IT2102.1 (or copy 1 of Optional Form W-2) and transmittal Form IT2102.4 if at least one individual was paid $600 or more.

- Also deadline for filing Federal Forms 1096 and 1099 when at least one individual was paid $600 or more in interest or rent.

**April 15** - Deadline for filing final Federal and State income taxes and New York State unincorporated business tax for farmers who filed estimates by January 15.

Month-End Check - Any farm employer withholding Social Security taxes from hired men's wages must check at the end of each month to see if he has accumulated $100 in withholding and employer's contributions of all employees. If so, the total amount accumulated is to be deposited at any Federal Reserve Bank or authorized commercial bank by the 15th of the following month. Federal Reserve Form 511 is used for this purpose.

* When a tax filing date falls on a Saturday, Sunday, or legal holiday, the filing may take place on the next day which is not a Saturday, Sunday or holiday.
TAX FORMS NEEDED BY NEW YORK FARMERS

Federal Forms
1040 - U. S. Individual Income Tax Return
Schedule C (Form 1040) - Profit (or Loss) from Business or Profession
Schedule D (Form 1040) - Gains and Losses from Sales or Exchanges of Property
Schedule F (Form 1040) - Schedule of Farm Income and Expenses
1040 X - Amended U. S. Individual Income Tax Return
1065 - U. S. Partnership Return of Income
Schedule D (Form 1065) - Gains and Losses from Sales or Exchanges of Property
3468 - Computation of Investment Credit
4136 - Computation of Gasoline Tax Credit
W-2 (or Optional Form W-2) - Wage and Tax Statement
W-3 - Transmittal Form
1096 and 1099 - Information Returns
Form 943 - Employer's Annual (Social Security) Tax Return for Agricultural Employees

New Federal Forms
Revision of Form 1040 and supplemental schedules has brought the development of the following new forms. The 1040 SE will be used by all farmers. Other new forms will be used by some farmers.
1040 A - Form for Itemizing Deductions
1040 T - Computation Form
1040 E - Supplemental Income Including Rent
1040 R - Retirement Income
1040 B - Dividends and Interest
1040 SE - Computation of Self Employment (Social Security) Tax

New York State Forms
IT-201 - Individual or Joint Return
IT-208 - Combined Income Tax Return
IT-204 - Partnership Return (Income and Unincorporated Business Tax)
IT-202 - Unincorporated Business Tax
IT-2102.1 - Information Return (or use Optional W-2)
IT-2102.4 - Transmittal Form
TAX REFORM AND FARM TAX REPORTING

Tax reform proposals have received much publicity in 1969, and tax reform apparently will continue to be in the news in early 1970. Most of the proposed changes will not affect 1969 farm tax returns. One exception is elimination of the tax investment credit. It is expected that the credit will be eliminated effective April 18, 1969. Other than the investment credit elimination, the most striking change effective for 1969 returns concerns the forms to be used. Form 1040 and supporting schedules have been greatly changed. Schedule 1040 F has also been rearranged.

Tax reform has been a major goal of the present administration. Here is the major sequence of events showing progress through 1969:

February - House Ways and Means Committee published a report of a two year study on needed tax reforms.

April - President made a statement to Congress urging adoption of several Treasury Department reform measures, elimination of investment credit, and continuation of surtax.

August - House passed H.R. 13270, a tax reform act, with sweeping changes affecting most taxpayers.

September - Treasury criticized H.R. 13270, offered alternative reform measures.

October - Senate Finance Committee completed revision of H.R. 13270 and offered a proposal to the Senate as a whole.

Late November - Senate prepared to debate proposed tax reform act.

It could be several months before a comprehensive tax bill is passed, but it seems likely it will be done early in 1970.

Many of the proposed changes would affect farmers. Some are aimed specifically at farmers and farm tax reporting. Though few will affect 1969 returns, good tax management dictates a need to keep informed about the proposed changes.

**Suggested Changes of Greatest Importance to Farmers**

Among the proposed changes which are of great importance to farmers are the following:

**Investment Credit Repeal** - All major proposals for tax changes have suggested elimination of the credit as of April 18, 1969. Probably this change will cost farmers more tax dollars than all other suggested changes combined.
Treatment of Gain on Sale of Livestock - Inclusion of livestock in 1245 property would change treatment of gain realized on sale of purchased livestock held for dairy or breeding purposes. Such gain is now capital (hybrid) gain, and would, after 1969, be ordinary gain.

Example: A dairy farmer purchases a cow and holds her three years for dairy purposes. Purchase price $400, depreciation taken, $300, sale price $300. The gain of $200 is now eligible for capital gain treatment. Under the proposed change, such gain will be ordinary to the extent of depreciation taken after 1969.

Holding Period For Livestock Increased - The current 12 months holding period for livestock would be increased, probably to two years. The longer period would be required in order to qualify income from sale as capital gain.

Example: A dairy farmer raises five heifer calves, expecting to add them to his dairy herd. After they reach 12 months of age, he finds he will not need them as herd replacements, so sells them. Currently, the income is eligible for capital gains treatment, as his intent was to hold the animals for dairy purposes. Under a proposed change, the income would be ordinary, as he held the animals less than two years.

Farm Losses - Taxpayers with over $50,000 of nonfarm income would be limited to deductions for farm losses to $25,000, plus $25,000. Additional losses could be carried forward to offset farm income only. Farm corporations, regardless of nonfarm income, would be limited to $25,000 farm losses plus $25,000 of the excess.

Capital Gains - Long term capital losses would be reduced by one-half before offsetting gains, corporate capital gains tax rate would increase to 30% in future years, and high bracket taxpayers will have less favorable treatment on capital gains.

Income Averaging - Procedure is to be simplified, and more income is eligible for averaging. Averageable income will be all over 120% of base period income instead of current 133 1/3%.

Hobby Losses - The definition of hobby farming would be more restrictive under a proposed change, providing fewer opportunities for taxpayers to "farm for fun" and use losses to offset nonfarm income.

Real Estate Depreciation - Fast depreciation on real estate would be denied on new construction, and the percentage reduction for depreciation recapture which is now in force (section 1250) would be eliminated.

Crop Insurance Proceeds - Would allow crop insurance proceeds to be reported in year of loss or in following year, if crop would normally have been sold in following year.

Some of these proposed changes will probably be revised or eliminated before tax reform becomes reality.
INVESTMENT TAX CREDIT

Status of Investment Credit

It is not known as of date of publication whether the tax investment credit will be available on property acquired after April 18, 1969, or with respect to property where the construction, reconstruction, or erection occurred after that date. It is certain that the status of the investment credit will be well publicized prior to tax reporting time. In any event, the tax credit is available on property acquired between January 1 and April 18, 1969. Some taxpayers will have unused credit from former years to apply against 1969 tax. Property disposed of in 1969 will in some instances, result in recapture of credit taken in previous years.

Limitations on Investment Credit

Total investment credit which may be taken is limited to the amount of the tax liability up to a maximum of $25,000. When the tax liability is more than $25,000, investment credit is now limited to $25,000 plus 50 percent of the excess over $25,000.

The investment credit may not be taken on more than $50,000 worth of used assets in any one year.

Property does not qualify if used by a relative before its present acquisition. This includes spouse, ancestors and lineal descendants, but not a brother or sister.

Property Which Qualifies

Each year some additional clarification is gained on qualifying property. In general, the credit applies to any depreciable property used in farming except livestock, buildings and most structural parts of buildings.

Machinery and equipment items are clearly eligible. These include not only the common movable items such as tractors, planting equipment and combines but also such stationary items as pumps, stanchions, feed bunks, and materials handling equipment. Two-way radios, farm office equipment and an airplane used in the farm business will also qualify. If items qualify except that they are partly for personal use, claim investment credit only on the business share.
I.R.S. has been very reluctant to classify any farm storage, other than grain bins and silos, as eligible for the investment credit. Any storage facility which looks like a building is likely to be classified as a building by I.R.S. However, a storage facility, such as a modified air fruit storage, which has no other use and could not be readily adapted to other uses, appears to qualify under the regulation.

On items where there is some question as to the eligibility, it would seem that the taxpayer's best course is to claim the credit and await events.

**Computing The Qualified Investment**

The investment tax credit is 7% of the "qualified investment" on eligible property. On a straight purchase of a new or used item of property, the qualified investment is simply the price paid. However, in the case of certain trades, exchanges, or replacement transactions, calculation of the qualified investment becomes complicated.

It is also necessary to keep in mind that when useful lives of less than eight years are estimated, only part of the 7% credit is available.

The following examples will provide practice in determining the qualified investment.

<table>
<thead>
<tr>
<th>Transaction</th>
<th>Qualified Investment</th>
<th>Rule</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. New tractor purchased for $6,000, estimated useful life 10 years, no trade involved.</td>
<td>$6,000</td>
<td>On purchase of new or used property without a trade-in, qualified investment is the cost.</td>
</tr>
<tr>
<td>2. Used tractor purchased for $3,000, estimated useful life 5 years, no trade involved.</td>
<td>$1,000</td>
<td>Same as 1, but estimated life of 5 years limits qualified investment to 1/3 of cost.</td>
</tr>
<tr>
<td>3. New tractor acquired for $3,000 cash and an old tractor with a basis of $1,500. Estimated useful life of new tractor, 10 years.</td>
<td>$4,500</td>
<td>On a non-taxable exchange, basis for investment credit is the sum of cash paid and adjusted basis of traded-in item.</td>
</tr>
<tr>
<td>4. New tractor acquired for $3,000 cash, and livestock traded-in with adjusted basis of $2,000 but market value of $3,000. Estimated useful life of tractor, 10 years.</td>
<td>$6,000</td>
<td>On a taxable exchange, basis for investment credit is cash plus fair market value of traded-in items.</td>
</tr>
</tbody>
</table>
5. Used tractor acquired for $3,000 cash and old tractor traded-in with adjusted basis of $1,000, estimated life of newly acquired tractor, 5 years.

$1,000

When used property exchanged for used property in a non-taxable exchange, adjusted basis of traded-in item not included in basis for investment credit. Five year life limits credit to one-third of cash paid.

6. A used tractor was purchased for $4,000 to replace a used tractor which was sold separately. The tractor purchased has estimated life of 5 years. The tractor sold had adjusted basis of $1,000.

$1,000

When a used item is purchased to replace a used item which was sold, cash paid for the newly acquired item must be reduced by the adjusted basis of the item sold, if the two are "similar or related" in service or use.

In addition to the six transactions illustrated, a special rule is invoked with respect to investment credit when a casualty or theft loss occurs.

Assume that a tractor with an adjusted tax basis of $4,000 is completely destroyed by fire. Tax investment credit of $420 had been taken on this tractor just two years before (cost $6,000). Subsequent to the fire, $3,000 insurance was collected.

The rule which applies is: If neither the insurance collected nor the adjusted basis of the lost item exceeds the reduction in the amount originally subject to investment credit on the lost item, the recapture rule applies:

**Lost item - Tractor, cost $6,000, estimated life 10 years, amount originally subject to investment credit $6,000, tractor burned after two years, insurance collected $3,000, adjusted basis $4,000, reduction in amount subject to investment credit $6,000.**

In this case, the entire amount of investment credit, ($420) taken at purchase of the tractor, is recaptured, and added to the tax in year of the casualty loss. If a tractor is purchased to replace the lost one, investment credit is calculated on it without reference to the casualty loss.

If the reduction in the amount subject to investment credit on the lost item is exceeded by either the insurance collected or the adjusted basis of the lost item or both, then the casualty or theft rule applies:

**Lost item - Tractor, cost $6,000, estimated life 4 years, amount originally subject to investment credit $2,000, tractor burned after two years, insurance collected $3,000, adjusted basis $4,000, reduction in amount subject to investment credit $2,000.**

In this case, the investment credit originally taken is not recaptured, but the basis of a tractor purchased to replace the lost one must be reduced by $3,000 for calculating investment credit, the lesser of the two items of insurance collected and adjusted basis. If the insurance collected was $3,200 then the basis of the replacement tractor must be reduced by $4,000 before calculating investment credit.
The Recapture Rule

If you dispose of an asset before the expiration of the useful life on which the credit was computed, you must recompute the amount of the investment subject to the credit. If the recomputed credit is less than you have used to reduce your tax, you must add to your tax liability in the year of disposition, the difference between the credit taken and the credit earned.

Example #1: In 1964, you purchased a tractor for $6,000, estimating a useful life of 10 years. On the 1964 return, you calculated the credit as 7% of $6,000 or $420. You had a tax liability before the credit of $1,000, so applied the entire $420 to tax reduction in 1964.

In 1969, you sold the tractor, having kept it more than 4 years, but less than 6 years. Its useful life in your hands thus entitles you to a credit of 1/3 of 7% of its cost, or $140. The difference between the amount taken ($420) and the amount earned ($140) is $280, which must be recaptured. You attach a statement explaining the transaction, to Form 1040 and enter $280 on Line 14b, Page 1, Form 1040, as an addition to tax.

In disposing of an asset before the expiration of its useful life, you may find that the credit earned is more than you have actually used to reduce your tax.

Example #2: In 1968, you purchased a tractor for $6,000, estimating a useful life of 10 years. On the 1968 return (Form 3468), you calculated the credit as $420. However, you had no income tax to pay in 1968, and did not use the $420 to recover tax in former years through carry-back. Therefore, you added the $420 to unused investment tax credit.

In 1969, you disposed of the tractor. Having kept it less than 4 years, no credit has been earned. Because no part of the $420 was used to reduce tax, no recapture results on the 1969 return. However, unused credit must be reduced by $420.

What Is A Disposition?

When you cease to own the property or cease to use it in a qualifying manner, you have disposed of it for purposes of the tax credit. If you sell it, exchange it, give it away, contribute it to a partnership, burn it up, or get rid of it through liquidation, you have disposed of it, and must recompute the credit. If you die before the end of the useful life of the asset, no adjustment is necessary.

Problems relative to investment credit have arisen in initiating farm partnerships between father and son. If, in doing so, the father sells a share of or full ownership of assets to the son which have been subject to investment credit, the father must recompute the credit on the items thus disposed of, which may result in the recapture of a significant amount of investment credit. The son as purchaser, however, is not allowed the credit, because the credit is denied on all property acquired from a close relative.

It may be advisable in family transactions to lease rather than sell the assets which have been subjected to the credit.
DEPRECIATION

Depreciation records are becoming more and more important in the preparation of accurate farm income tax reports. Copies of past returns do not provide sufficient information for complete and accurate reporting on most commercial farm operations. A separate more detailed depreciation record such as the one illustrated in the Farmers Tax Guide is suggested.

**Item vs. Class Reporting**

Entries on the depreciation schedule may be summarized into distinctly different classes of depreciable assets. However, the taxpayer must have his own records kept in enough detail to verify the accuracy of the summarized schedule.

In most cases, it is probably best for a farmer to continue to use item accounts rather than grouping machinery, buildings, or cattle. A separate continuation sheet of Part V - Depreciation may be attached to Schedule F if more lines are needed.

**Depreciation Guidelines**

Internal Revenue Service Publication 456 includes guidelines for determining reasonable useful lives of depreciable farm business property. These include:

A. Machinery and Equipment - 10 years

B. Animals:
   - Cattle, breeding or dairy - 7 years
   - Hogs, breeding - 3 years
   - Sheep and Goats, breeding - 5 years

C. Farm buildings - 25 years

For many classes of depreciable property, no specific useful lives are suggested, and statements are made that the facts in each case should determine the depreciable life. Depreciation rates should be set in line with experience on the farm of the taxpayer. IRS Publication 456 says,

"The determination of the useful economic life of an asset is a matter of judgement and estimate. For this reason, it is the policy of the Internal Revenue Service, generally, not to disturb depreciation deductions. Therefore, adjustments in the depreciation deduction should not be proposed unless there is a clear and convincing basis for a change."

**Depreciable Real Estate**

Farmers who purchase property frequently overlook their opportunity to claim depreciation on depreciable real estate items included in the purchase and used in the farm business. In addition to farm buildings, these might include fences, drain tiles, drilled wells, and commercial orchards or vineyards (investment in trees or vines and trellis aside from the value of the bare land). Such expenditures are also eligible for the investment tax credit.
It is important that the taxpayer keep a record of real estate purchases and of his allocation of the purchase price to land, buildings and other depreciable portions of the cost.

If an orchard or vineyard has been grown or a fence erected by the present owner and the costs deducted on previous income tax returns as annual operating expenses, then depreciation may not be taken because the costs have already been charged off.

Recovering Costs of New Orchards and Vineyards

Amounts spent in setting out new orchards and vineyards must be treated as capital investments rather than as current operating expenses.

The taxpayer may treat as either capital investment subject to depreciation or as current operating expense such expenditures during the development period of orchards and vineyards as those for cultivating, spraying, pruning, and taxes. Some farmers have found it convenient to treat these expenditures as current operating expenses.

Because the investment in orchards and vineyards has been ruled eligible for investment tax credit, farmers have an incentive for capitalizing the costs involved in establishing new orchards and vineyards. The costs to be capitalized are eligible for the investment tax credit the year in which the orchard or vineyard comes into production.

Economics of Rapid Depreciation

Farmers generally use straight line depreciation because of its simplicity. For farmers who do have sizeable taxable incomes, the savings through fast depreciation should not be overlooked. By combining the 20% first year special allowance with double declining balance, much of the tax reduction through depreciation can be crowded into the first years of ownership, which results in postponing tax. Even when a conservative value is placed on the use of those postponed tax dollars by the farmer, a significant saving results.

Power equipment and harvesting equipment costing $10,000-$25,000 is no longer unusual. A farmer in the 32% tax bracket who purchases a harvesting machine for $20,000 with an expected life of eight years stands to save $500-$600 if he chooses 20% special and double declining balance over straight line depreciation.
### Guidelines for Depreciation for Farm Assets

<table>
<thead>
<tr>
<th>Description</th>
<th>Additional 1st. Yr. Dep.</th>
<th>Depreciation Methods</th>
<th>Suggested Life</th>
<th>Basis for Computing:</th>
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<tbody>
<tr>
<td><strong>NEW MACHINERY PURCHASED</strong></td>
<td>Yes - 6 yrs. or more life</td>
<td>St. Line - yes D. Bal. - 3 yrs. or more life. Digits - 3 yrs. or more life.</td>
<td>10 Yrs.</td>
<td>Boot paid plus undep. balance on trade less add. lst. yr. dep. less required salvage val.</td>
</tr>
<tr>
<td><strong>USED MACHINERY PURCHASED</strong></td>
<td>Same as above</td>
<td>St. Line - yes D. Bal. - 3 yrs. or more life and limited to 1/2st. life rate. Digits - no.</td>
<td>No Guide</td>
<td>Same as above</td>
</tr>
<tr>
<td><strong>NEW BUILDINGS</strong></td>
<td>Not eligible</td>
<td>St. Line - yes D. Bal. - 3 yrs. or more life. Digits - 3 yrs.</td>
<td>25 Yrs.</td>
<td>Cost</td>
</tr>
<tr>
<td><strong>USED BUILDINGS PURCHASED</strong></td>
<td>Not eligible</td>
<td>St. Line - yes D. Bal. - 3 yrs. or more life and limited to 1/2st. life rate. Digits - no.</td>
<td>No Guide</td>
<td>Same as above</td>
</tr>
<tr>
<td><strong>FENCE, SILOS, GRAIN STORAGE, DRAIN TILES</strong></td>
<td>Not eligible</td>
<td>St. Line - yes D. Bal. - 3 yrs. or more life. Digits - 3 yrs. or more life.</td>
<td>25 Yrs.</td>
<td>Cost</td>
</tr>
<tr>
<td><strong>BREEDING AND DAIRY ANIMALS PURCHASED</strong></td>
<td>Yes - 6 yrs. or more life (except limited to 1/2st. line rate on d. bal. for livestock)</td>
<td>Same as above.</td>
<td>3-10 Yrs.</td>
<td>Boot paid plus undep. balance on trade less lst. yr. dep. less salvage value.</td>
</tr>
<tr>
<td><strong>FRUIT TREES AND VINES</strong></td>
<td>Not eligible</td>
<td>Same as above.</td>
<td>No Guide</td>
<td>Cost</td>
</tr>
</tbody>
</table>

<table>
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<tr>
<th>Add. lst. 1st. Yr. Dep.</th>
<th>Boot only</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost less salvage value</td>
<td>Not eligible</td>
</tr>
<tr>
<td>Not eligible</td>
<td>Not eligible</td>
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<tr>
<td>Not eligible</td>
<td>Not eligible</td>
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CAPITAL GAINS AND LOSSES

For income tax purposes, property owned by farmers can normally be classified as capital assets, non-capital or ordinary assets, and hybrid assets that are sometimes treated as one and sometimes treated as the other, depending on the circumstances. Hybrid assets can be further divided into Section 1231, 1245 or 1250 property.

Capital assets includes almost all property owned for non-business or personal use like stocks and bonds for investment, residence, car, etc.

Non-capital assets is property held for sale in the usual operation of the farm business. Apples, potatoes, feeder cattle, feeder lambs, bob calves, and poultry, are never capital assets.

Items that sometimes are, sometimes are not, treated as sales of capital assets can for convenience sake be called hybrid items. They include:

A. Sales, exchanges, involuntary conversions (except for uninsured casualty and theft losses) of:

(1) Livestock held for draft, dairy, or breeding purpose for one year or more.
(2) Farm land held for more than six months.
(3) Machinery held for more than six months (except that gain on such items to the extent of depreciation occurring after 1961 will always be ordinary gain).
(4) Farm buildings held for more than six months, except that part or all of the gain which can be attributed to depreciation may be ordinary assets.

B. Gains and losses arising from fire, theft, or condemnation of capital assets.

C. Casualty losses of insured property.

D. An unharvested crop sold with the land, when the land has been held for more than six months.

The farmer must compare gains and losses of these items. If the comparison shows a net loss, none of them are treated as capital gains. All are then entered as ordinary gains and losses under "Property Other Than Capital Assets," on Schedule D, Part III except casualty losses on assets such as a boat, auto for personal use, etc. These are listed on page 2 of Form 1040, if deductions are itemized. If the gains exceed the losses, all the gains and losses are listed in Part I, line 5 of Schedule D.

All sales of livestock held for draft, dairy, or breeding purposes are listed on Schedule D, as follows:

* The treatment of income from sale of livestock held for dairy or breeding purposes is expected to change for tax years commencing after December 31, 1969
A. In Part I, line 5, if held for a year or more and there is a gain on these hybrid items that sometimes are and sometimes are not treated as sales of capital assets:

or

B. In Part III, line 1, page 2 of Schedule D, if held for less than one year or if there is a net loss on these items.

Casualty and theft losses of animals held for dairy or breeding purposes for less than one year and of farm buildings and machinery held for six months or less are always listed in Part III, page 2 of Schedule D.

A casualty or theft loss, not compensated for by insurance in any amount, of purchased livestock held 12 months or more for draft, dairy, or breeding purposes, or of other depreciable farm property held more than six months, is treated as an ordinary loss, deductible in full, and is always listed in Part III, page 2 of Schedule D as "Property Other Than Capital Assets."

The Rule on Gain Realized From Sale of Farm Machinery (Section 1245 Property)

Gain on sale of all depreciable personal property except livestock, and all other tangible depreciable property except buildings is ordinary gain to the extent of depreciation allowed or allowable on such property after 1961.

This rule is designed to discourage farmers from depreciating a farm machine rapidly, selling it at a "profit" which is only 50% taxable, then buying a new machine and receiving the investment credit.

The rule affects such property disposed of in any tax year commencing after December 31, 1961.

The rule is effective only to the extent of depreciation allowed or allowable after 1961 on each item concerned.

The rule does not apply to any livestock or to buildings.

Relatively few farmers are affected, because in the normal course of events, farmers trade in used machinery and equipment, they do not sell outright. In the instances where used farm machinery is sold outright, it probably results in a loss as often as in a gain.

Where farm machinery is sold or otherwise disposed of in a way which results in recognizable gain or loss, the disposition is reported as follows:

A. If there is any gain on such items, the disposition is reported in Part II, page 1, Schedule D. The extent of the gain which is ordinary is determined there.

If the calculation in Part II shows that some of the gain may be capital, that amount is included with other hybrid assets in the comparison to determine net gain or net loss from all such hybrid assets.
B. If there is a loss on disposition of such items, they are included in the group of hybrid assets in the comparison to determine net gain or net loss from all such hybrid assets.

The Rule on Gain From Sale of Farm Buildings (Section 1250 Property)

Rule changes made in 1964 affect classification and reporting of gain realized from the sale of depreciable realty used in the business, called Section 1250 property. Few farm sales are affected, because a majority of farmers use only S-line depreciation on farm buildings.

If the property is held for at least one year and only S-line depreciation is taken after 1963, no adjustment is necessary, all gain is capital gain as formerly.

If property is held for 10 years or more, no adjustment is necessary, regardless of the method of depreciation used.

If property is held for one year or less, gain in the amount of all depreciation taken including that taken under S-line, is ordinary gain.

If property is held for more than one year but less than ten, a "fast" method of depreciation is used, and gain is realized on the sale, the gain must be divided.

1. Determine total gain realized on sale of the depreciable real estate.

2. Determine the amount of additional depreciation taken in excess of S-line.

3. Determine "applicable percentage" - 100% minus 1/3 per month for each month the property is held over 20 months.

A percentage of the lesser of 1 or 2 is treated as ordinary income, and to determine the percentage, step 3 must be taken.

Assume a farm is sold after being held five years. Allocation of sale price shows gain on depreciable farm buildings of $5,000. The farmer was using the declining balance method of depreciation, which resulted in $2,000 more depreciation than would have been taken with S-line during the five years of ownership.

The "applicable percentage" in this case is 60%, because the property was held 40 months over the 20 month period. (100% - 40% = 60%)

In this case, the excess depreciation ($2,000) is less than the amount realized over the adjusted basis ($5,000), so 60% x $2,000 = amount to be treated as ordinary gain.

Gain from sale of Section 1250 property must first be reported in Part II, Page 1, Schedule D. That part of the gain there found to be "other gain" is then included in hybrid assets. If there is a loss on sale of Section 1250 property, the loss is included in the group of hybrid assets.
TAX SAVINGS IN TRADING FARM PROPERTY

If farm business property is exchanged for farm or other business property, all or part of the gain can escape immediate taxation. The special tax treatment available in tax free exchanges is not commonly understood by farmers. As a result, farmers often make sales of property which they mistakenly believe qualifies as a trade or swap. On the other hand, farmers sometimes fail to take advantage of the opportunity to make a trade instead of making an outright sale, and thus incur heavy current taxes which could have been postponed.

A Simple Nontaxable Exchange Illustrated

Suppose a farmer decides to retire and liquidate his farm business. He has an offer of $100,000 for his farm real estate, which has an adjusted tax basis of $30,000. If he makes an outright sale for cash he incurs a gain of $70,000, of which $35,000 is taxable. He can, of course, ease his tax problem by selling on the installment basis. He might also be able to arrange a tax free exchange. Suppose he is selling to a real estate developer who owns an apartment house which he will sell for $100,000, or will trade even for the farm. If the farmer trades with the developer, he ends up owning an apartment house with an adjusted tax basis of $30,000, and has no gain to report in the year of the trade. He has postponed his tax problem, but has not eliminated it. However, he may be ahead with the trade. He may be able to dispose of the apartment house sometime in the future when other taxable income is less. Buying the apartment house may provide him with the kind of nonfarm investment which he wants.

Basic Rules to Qualify

- Both real estate and personal property will qualify for a nontaxable exchange.

- Property held must be "for productive use in a trade or business or for investment". Farm property qualifying would include farm land and buildings, livestock and equipment.

- The property exchanged must be of a "like kind". For real estate, the "like kind" rule is very flexible. Any income producing real estate may be exchanged for any other income producing real estate. Therefore, farm real estate may be exchanged for city real estate, such as an apartment, or for timberland, etc. The like kind rule for non-real property is much more restrictive. Dairy cows can be swapped only for dairy cows, farm equipment only for farm equipment. Some livestock owners have assumed that it is permissible to trade heifers for steers. Although the law is unclear, it appears that this interpretation is too broad.

- The exchange must be a direct one. No third party can be involved in ownership at time of trade. Selling a herd of cows to one or several persons, then buying back a replacement herd is not a nontaxable exchange. A farmer who wishes to swap his farm real estate for an apartment house in town must find an apartment house owner who wants to own a farm. However, "arranging" such an exchange is permissible. A farmer located in an area being developed for industrial purposes can say to the developer who offers him $100,000 for his farm, "you go buy a farm 200 miles from here and we'll work out a swap".
- The property received in the trade must be acquired for use in a business or for investment. A farmer who acquired an apartment in exchange for a farm with the idea of immediate resale of the apartment would not qualify

Some Gain May be Recognized in a Trade

If the trade is not even, if cash is received, or if the property traded or received is mortgaged, part of the gain may be recognized and immediately taxable in an exchange - examples are:

A farmer who trades a farm for an apartment house and pays cash in addition adds the cash payment to the adjusted tax basis of his farm to determine the tax basis of the apartment house, but has no gain to recognize.

If the farmer receives cash for his farm in addition to other investment property (the apartment house), the cash received must be reported as gain, up to the amount of gain which has occurred on the farm.

If a farmer trades his farm for an apartment house, with no cash involved, but in the deal the farmer is relieved of a $10,000 mortgage on the farm, and assumes no mortgage on the newly acquired property, he is considered to have received $10,000 in money for tax purposes.

Installment Sale May be Combined With Nontaxable Exchange

A transaction which involves a swap of property plus some cash or "boot" may qualify as both a nontaxable exchange, and as an installment sale. A farmer might trade his $100,000 farm for a $30,000 rental property plus $70,000 in addition, to be paid in installments of $10,000 a year. If the farm had a basis of $20,000, he would realize a gain of $80,000, but only $70,000 is recognized. Because the contract price is $100,000 and the recognized gain is $70,000, he would report 70% (70 : 100) of his cash payments each year as taxable gain. Each annual payment of $10,000 would thus result in taxable gain of $7,000. The rental property received in exchange would have a basis of $20,000.

Tax Free Exchange is a "Disposition" for Investment Credit Purposes

Property disposed of in a swap may result in investment credit recapture. Investment credit previously taken on the traded-in property must be recaptured if the property was not held for the required length of time to "earn" the credit.

Where Farmers May Benefit

There are probably few instances where farmers can materially benefit by arranging tax free exchanges of machinery or livestock. The usual method of trading used farm equipment for new farm equipment is a nontaxable exchange anyway, and there are no obvious ways of capitalizing on equipment swaps. The swapping of livestock would not be beneficial for many dairy farmers. A continuance of trading rather than selling would reduce the amount of income which qualifies for capital gain treatment.

The most likely opportunities for tax benefits from nontaxable exchanges are associated with disposition of farm real estate. When the potential gain on the sale of a farm is great, and when the farmer is interested in finding a substitute investment in other real estate, then he should carefully examine the possibility of exchanging his farm for other real estate instead of selling it and then looking for a place to invest the proceeds of the sale.
INCOME FROM WOOD, TIMBER AND CHRISTMAS TREE SALES

The easiest way to report farm sales of wood and timber is as ordinary income on Page 1, Schedule F. If the wood and timber sold was purchased standing at a previous date, depletion should be taken as a farm expense also on Page 1, Schedule F to help offset the income.

Generally, only those who want to increase farm income for Social Security purposes will find it advantageous to report sales of any substantial quantity of wood and timber as ordinary income.

Treating Receipts From Sale of Wood and Timber as Capital Gain

Income from the sale of standing timber owned more than six months and sold on the stump on a lump-sum basis, may be treated as a capital asset and the transaction reported under long-term capital assets on Schedule D.

Income from the sale of standing timber owned more than six months and sold on a cutting contract or pay-as-cut basis, is grouped with other "hybrid" items. If total gains exceed total losses, all these items are entered on Schedule D under long-term capital gains and losses. If total losses exceed total gains, all items are listed on Schedule D under property other than capital assets. (Part III)

When a farmer cuts wood and timber from his own land and sells the products, he may treat income as two separate deals. He can proceed as though he sold the standing timber to himself and report any gain as income from sale of a capital asset. Then when he sells the logs or wood, any "profit" realized on the cutting and selling deal is ordinary income.

Income From Sale of Christmas Trees

Christmas trees which are more than six years old when cut are considered the same as wood and timber for tax purposes. Here is an example where trees were raised, cut, bundled, and sold at the roadside by a farmer:

Value of 1,000 trees, on stump $800
Cost of trees and planting (all yearly growing costs were taken on annual tax returns when they occurred) 100
Capital gain on growing operations $700

Proceeds from sale of trees at roadside $1,100
Less fair market value of trees on stump 800
Less expenses for cutting, bundling and hauling 200 $1,000

Ordinary income from harvesting $100
Land Clearing Expenses

Since 1962, farmers have been allowed to treat land clearing costs as deductible expenses, rather than capital charges. Such expenditures must be for the purpose of making the land suitable for farming, and are limited to $5,000 or 25 per cent of taxable income whichever is lesser.

This rule is separate and apart from the soil and water conservation expense rule. Not many New York farmers are affected. It is likely that expenses of this kind have been classified as soil and water conservation expenses by many farmers in the past, and written off as an annual expense.

Farm Partnerships

For federal income tax purposes a partnership is generally said to be created when two or more persons join together for the purpose of carrying on a trade or business, including farming. Each partner contributes in some way -- either money, property, labor, or skill -- and shares in the profits or losses or both in accordance with agreed proportions.

Reporting

A partnership, as such, does not pay any income tax but must file an information return on Form 1065 for federal income tax, even though the partnership has no net income. These forms show what the income of the partnership is and how the income is divided between the partners.

Schedule F should be used to calculate the net farm profit and a copy attached to both the state and federal partnership return.

Each partner files his own Form 1040 after he enters his share of the partnership net profit. It is not necessary for the individual partners to file copies of either Form 1065 or of Schedule F.

Capital gains and losses of the partnership are filed on a special Schedule D (Form 1065) then each partner reports his share on Schedule D (Form 1040).

A partnership is not required to file Form 3468, investment credit, but is required to file a statement showing partnership items on which the credit was taken and how it was divided between the partners.

Balance Sheets, Form 1065

The partnership return calls for Balance Sheets (Schedule F) and Reconciliation of Partner's Capital Accounts (Schedule M). Most farm partners file on the cash basis and do not keep books of account which provide information for completing these two schedules. This information has no direct connection with the computation of taxable income. Internal Revenue asks for it merely to get a better picture of partnership operations. It is best to complete these schedules if possible. Most partnerships can complete the balance sheets as they would a credit statement. If the schedules cannot be completed, it is probably advisable to attach a brief explanation.
TAX CONSIDERATIONS IN INCORPORATION
OF THE FARM BUSINESS

Interest in the family or close-held corporation as a farm business arrangement has increased in the past few years. This interest is largely due to bigger businesses and more attention to income tax management.

Probably less than two percent of all commercial farms in New York are incorporated, but the number has been increasing. The corporate structure offers several possible advantages not related to tax management. Perhaps the most important is flexibility of property ownership represented by shares of stock, which can be easily transferred from one family member to another. However, many if not most farm corporations which have been formed recently have been created primarily as a way to save taxes.

There are several things to keep in mind in studying potential tax savings resulting from incorporation of farm business. First, only relatively large farm businesses with assets of $200,000 or more are likely to benefit. Secondly, only farm businesses with above average taxable incomes, stand to benefit. Thirdly, stockholders are usually only those family members who are actively engaged in the farm business. Fourthly, the type of corporation created can almost always qualify as a Subchapter S or 1120 S corporation. But if the choice is made to file as a Subchapter S corporation, some of the tax advantages sought by incorporating are lost. This is true because the 1120 S corporation is treated much like a partnership for Federal Income Tax purposes. Therefore, in citing tax considerations in incorporating, reference will be made to a regular 1120 corporation rather than to an 1120 S corporation.

Corporate Tax Rates Differ From Individual Tax Rates

Under current tax rate schedules, corporations are taxed at 22% on the first $25,000 of taxable income and 48% on all above. Individual tax rates start at 14%. For married taxpayers filing joint returns, the rate does not reach 22% until taxable income reaches $8,000. The rate is above 48% when taxable income exceeds $44,000.

Taxing of capital gains also differs between the individual and corporate taxpayer. The individual pays tax on only 50% of his capital gain, and that 50% is taxed at whatever rate the individual taxpayer is paying on total taxable income. Thus a taxpayer in the 25% tax bracket pays 12½% tax on each $1 of capital gain. The corporation is taxed on capital gain at the same rate as ordinary income or at 25%, whichever is lower. Thus a corporation with combined ordinary income and capital gains of $25,000 or less pays at the rate of 22% for each $1 of gain.

The Corporation is a Taxpayer

In forming a corporation, a new taxpayer is created. This presents some advantages. First, at the time the corporation is formed, a choice is available relative to fiscal or calendar year, and as to cash or accrual tax reporting. A more important advantage is the flexibility provided in shifting income between the corporation and family members.
Family members employed by the corporation normally draw salaries. Although salaries must represent reasonable compensation for services performed, and must be set at the beginning of the year, considerable flexibility is allowed in setting salaries, and in declaring bonuses during the year. Thus income can be shifted between corporation and individuals to take advantage of lowest tax rates.

Some Expenses May be Shifted From Personal to Business

Some expenses which cannot be charged as business deductions in a farm partnership or individual proprietorship may be charged in a corporation. Many of these are associated with the farm residences. If the houses occupied by family members employed by the corporation are owned by the corporation, depreciation and maintenance on these houses may be charged as corporate expenses. They are, in effect, "tenant houses", occupied by the employee at the direction of and for the convenience of the employer. Under this rule, value of house rent is not taxable income to the employee. However, it may be undesirable for other reasons to have the corporation own the houses occupied by the family members.

Salaries or Wages to Various Family Members More Readily Substantiated

The formal structure of a corporation apparently makes it easier to justify payment of salaries to different family members. For example, accounting duties carried by a farm wife can justify a corporate salary. Even though the advantage for Federal Income Tax may be small or nil, there may be an advantage on State Income Tax, and also this opportunity adds to the flexibility available in drawing off corporate income.

Transferring Farm Property to Corporation Seldom Results in Taxable Gain or Loss

If a farm owner decides to form a corporation and transfer farm property to the corporation, the transfer is usually a nontaxable exchange. Therefore no taxable gain or loss results at the time of transfer. This is true because usually the person or persons who transfer property to the new corporation receive only stock in exchange and these individuals usually meet the requirement of owning at least 80% of the stock immediately after the transfer.

In such a transfer, the property has the same adjusted tax basis in the hands of the corporation as it had in the hands of the previous owner or owners. A herd of raised dairy cattle would retain a basis of zero in such a transfer and a set of farm equipment would have the same basis in the hands of the corporation as last reported on the farmer's depreciation schedule.

Withdrawing Income From a Corporation Requires Management

Close-held or family corporations usually do not pay dividends on corporate stock. If dividends are paid, double taxation results - first corporate tax on corporate profit, then tax to the stockholder when the dividend is paid. Double taxation does not occur when corporate income is drawn off as salaries to family members. A family member may be a creditor of the corporation. This provides an opportunity to draw off corporate income as interest payments.
In some cases less total tax results if the corporation is allowed to show a profit and to pay income tax. In such cases, it is assumed that a way will be found in future years to transfer these undistributed profits to stockholders under favorable tax conditions. Close-held corporations are generally not allowed to build up undistributed profits of over $100,000. In some very profitable farm businesses, this limitation has been one reason for forming two corporations - one to own the land, the second to operate the farm business, leasing the land from the first.

Family Members Employed by Corporation Have Different Tax Status

The farm family members who are employed by the family corporation have a new tax status somewhat comparable to any farm employee. The corporation as a "farmer" for tax purposes, is exempt from income tax withholding on employees, is responsible for social security withholding, is eligible for cash or accrual basis reporting, and is exempt from quarterly tax estimates if the February 15th date is used for the final return. The farmer himself, however, is no longer a "farmer" for tax purposes but is an employee of the corporation subject to the same rules on filing tax estimates and filing final returns as are other nonfarm taxpayers.

Deferred Taxation and Nontaxable Fringe Benefits of the Corporation

Farm family members may create an opportunity for deferred taxation fringe benefits by forming a corporation and becoming employees of that corporation. A corporation may establish a retirement plan for its employees, which can result in a reduction in tax to be paid on dollars placed in the retirement fund. Although it is true that a partnership or individual proprietorship can also do this, the rules governing corporate retirement plans allow more flexibility in method of funding the plan, in amounts which can be set aside, and in determining which employees are included.

The corporation also allows for the establishment of profit sharing plans and stock bonus plans which will provide deferred taxation for the employee.

In addition to these deferred taxation options, corporations can also provide important nontaxable fringe benefits to employees, including group health and accident insurance and group term life insurance.

Unfavorable Capital Gains Treatment Afforded Corporation May be a Problem

As has been pointed out, corporations do not receive a favorable treatment on taxable capital gains as to individuals, unless the individual is in the 50% tax bracket or above. A corporation therefore may be tax disadvantageous when the business at hand can expect significant income in the form of capital gains. For example, a dairy farmer in the 25% personal income tax bracket, operating as an individual proprietorship, selling $8,000 of raised animals held for dairy or breeding purposes each year, would normally pay $1,000 in Federal Income Tax as a result of these sales. If he switched to a corporation, he could expect to pay $2,000 in tax attributable to the same cattle sales. It should be pointed out that only dairymen with 150 cows or more, raising all replacements, would be likely to have sales of this magnitude. Also only livestock farms usually produce much income of this kind.
If farm land is transferred to a corporation, capital gains taxation takes on special significance. The market value of most farm land has increased considerably in recent years, and this results in a sizeable capital gain upon sale. For this reason, caution should be taken in transferring farm land with a low tax basis to a corporation where sale at much higher values is even a remote possibility in the near future.

Election to be Treated as a Subchapter S Corporation

If election is made to file for Federal Income Tax purposes as a Subchapter S corporation, the net income of the corporation is passed through to the stockholders proportionate to their shareholding. Capital gain of the corporation is also distributed in the same manner. The corporation files an information return, similar to the partnership return, but pays no tax itself.

Resort to the Subchapter S corporation removes the problem of higher capital gains taxation and the problem of distributing corporate earnings without double-taxation. It also would appear that the possibility of shifting some expenses that are definitely "personal" in an individual proprietorship to "business" exists for the Subchapter S as well as the regular 1120 corporation. However, one potentially great tax advantage - that of shifting income between individuals and corporation - is lost when the 1120 S corporation is elected. It is the reluctance to give up this flexibility which causes many farm corporations to elect to file as regular 1120 corporations.

Permission to change from reporting as an 1120 S corporation to an 1120 corporation and back again is restricted. The election of 1120 S reporting must be made within one month of the beginning of the tax year to be effected. It must be in effect at least one year before permission will be granted to switch to reporting as an 1120 corporation. Permission would then not be granted to change again to an 1120 S corporation for five years.

Federal Income Tax Law Governing Both Corporations and Unincorporated Businesses Change Over Time

One of the imponderables in weighing the tax savings from incorporation is the certainty that tax law will not remain static. What currently is an advantage for the corporation might disappear in the next revision of the Federal Income Tax Law, and there could be several such revisions over the life of one farm business. For example, one proposal for tax reform debated in Congress in 1969 to curb "Tax Dodge" farmers - people who enter farming expecting to use farm losses to offset nonfarm income - was much harsher on corporate farm taxpayers than on unincorporated farm taxpayers.

Although the relative tax treatment of corporate and unincorporated farm businesses is sure to change, selection of the corporate organization now does not eliminate the possibility of dissolving the corporation at some future date.

New York State Unincorporated Business Tax is a Consideration When Incorporating

When a New York farm business is incorporated, the effect is to exchange the New York State Unincorporated Business Tax for the New York Corporate Franchise Tax. This may result in a tax saving. This is best illustrated if it
is assumed that a very profitable unincorporated business is incorporated, then corporate taxable income is kept at or close to zero by drawing off income as salaries to family members. The result may be a small corporate tax in place of a sizeable unincorporated business tax.

Farm business partnerships are at a disadvantage under the unincorporated business tax. The unincorporated business tax provides an "allowance for taxpayer's services" of 20% of net income or $5,000, whichever is lower, and it allows an exemption of $5,000. A big farm business operated as a partnership to support three or more farm families must produce a significant amount of taxable income above these exemptions. Such a business gets no more exempt income under unincorporated business tax than a farm business owned and operated by one man. Thus a farm where two or more families are in partnership may gain by swapping the unincorporated business tax for the New York Corporate Franchise Tax. The calculation of the New York Corporate Franchise Tax is a complicated procedure. For planning purposes, it can be assumed that it will be $100 or 7% of corporate net income, whichever is higher.

Summary

The possibilities of saving income taxes by incorporating a farm business stem from these tax advantages:

- By forming a corporation, income may be shifted between individuals and the corporation to keep income in lower tax brackets.

- Some expenses which were previously nonbusiness may become business and deductible with a corporation.

- The corporation provides more opportunities for paying fringe benefits to employees which are nontaxable or on which taxation may be deferred.

- Tax saving may result from elimination of the New York State Unincorporated Business Tax.

In considering incorporation, these tax problems should be kept in mind:

- Taxation of capital gains is less favorable to a corporation than to an unincorporated business.

- Corporate earnings cannot be distributed to stockholders as dividends without double taxation of those earnings.

In weighing the tax advantages and disadvantages of a corporation, it should be recognized that a corporation offers nontax advantages as well as nontax disadvantages. The decision to incorporate should not be made solely on the basis of tax considerations.

The owner of any large and profitable farm business should examine the possibility of incorporating as a tax management measure. Substantial tax savings can be realized by a few good commercial farms.

This discussion of possible tax savings through incorporation of the farm business is very general. A farmer should obtain qualified professional assistance to determine how these points will affect his business and tax responsibilities.
SOCIAL SECURITY

Earnings Base

The maximum amount of earnings that can count for social security and on which you pay social security contributions was increased to $7,800 on January 1, 1968. This will not be changed for 1970.

SOCIAL SECURITY CONTRIBUTION RATES

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<th>Year</th>
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<td>Hospital OASI* insurance Total</td>
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* Federal Old-Age and Survivors Insurance Trust Fund and the Federal Disability Insurance Trust Fund

Farmer's Option

Farm operators are the only self-employed group covered by social security that have the privilege of an optional method of reporting earnings for social security. If a farmer's gross farm income is over $2,400 but his net earnings are less than $1,600, he may choose to pay the social security tax either on his actual net earnings or on $1,600. If his gross income from farming is not more than $2,400, he may elect to pay social security tax on 2/3 of his gross income. This option has the effect of providing minimum covered earnings of $1,600 per year for any farmer who has a gross income of $2,400 or more.

Because retirement, survivor and other benefits are computed on the basis of average earnings, farmers will almost always benefit by using the optional method in years of low earnings. In some cases, they will benefit greatly by doing so.

The optional method is recognition that farm earnings fluctuate widely from year to year. It provides a means for all commercial farmers to add to their social security earnings on a regular basis.
### RAPID CALCULATOR FOR SOCIAL SECURITY WITHHOLDING
1969-1970 - 4.8 Percent

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It is a farmer’s responsibility to make Social Security tax withholdings from wages or other compensation paid to any worker who earns $150 or more or who works a total of 20 days or more in any calendar year.

When accumulated deductions plus matching employer contributions reach $100 or more by the end of any month, these amounts must be deposited by the 15th of the following month with a Federal Reserve Bank or commercial bank authorized to receive them. Federal Tax Deposit Form 511 is used for this purpose. Under present procedures, taxpayers do not receive validated receipts to attach to their returns as evidence of payment.

The above rapid calculator may be of help in determining the withholdings to be made from an employee's wages.
FARM EMPLOYEES AND INCOME TAXES

Income Tax Withholding by Farmers Not Permitted

The law does not permit a farmer to withhold federal income tax from wages paid to his employees. The Internal Revenue Code specifically excludes withholding from wages of agricultural labor.

A few farmers and their employees have worked out their own plan whereby the farmer sets aside from the employee's wages an amount which is deposited in a savings account in the employee's name. This amount is then available to the employee to pay his income tax when due.

Farm Employer Must Report Earnings

A farmer must report all amounts of $600 or more paid to any one employee. Form W-2 or Optional Form W-2 are used for reporting the amount paid. The federal form must be filed by January 31, and the state form by February 28.

Farm Employee Must File Returns

A hired man with a gross income of $600 ($1,200 if over 65 years of age) or more is required to file an income tax return. These must be filed by April 15.

For federal income tax, a hired man may exclude from his gross income the value of any meals, lodging, or rental value of a house furnished to him by his employer for the convenience of the employer, but only if:

1. The meals are furnished on the business premises of the employer and for the employer's convenience.

2. Lodging or house rental where the employee is required to accept such lodging or housing on the business premises of the employer as a condition of his employment.

A farm employee is required to file a declaration of estimated income tax (Form 1040-ES) if his estimated tax is $40 or more. The tax may be paid in four equal installments which spreads the money needed for tax purposes throughout the year even though withholding is not permitted. Some employees have been penalized for not filing estimates.

Pay to Children

Farmers who pay their dependent children for work actually performed by them can save tax dollars by shifting income from themselves to their children. A child who earns $900 or less will not owe any federal or state income tax. If he is under 19 or a full-time student, he may still be a dependent if his parents provide more than half of his support. The wages paid to a child appear as a labor expense on the farmer's 1040F.
RETIREMENT INCOME CREDIT AND FARMERS

Few farmers, even in older age brackets, think of themselves as retired. Consequently, it is likely that a significant number of farmers who are eligible do not take advantage of the retirement income credit when they file their income tax returns. Older farmers should be acquainted with this tax credit.

How is Credit Figured?

A summary of the rules will help to indicate the circumstances under which farmers can benefit from retirement income credit.

- To qualify, a taxpayer must meet the "prior earned income test," must have received over $600 of earned income in each of at least 10 prior calendar years.

- Fifteen percent of eligible retirement income is allowed as a credit directly against income tax due. The total allowed cannot be greater than the tax due.

- The maximum amount of retirement income eligible for the 15 percent credit is $1,524. Fifteen percent of $1,524 is $229, which represents the maximum reduction in income tax possible for a taxpayer.

- If both taxpayer and spouse are eligible and each has retirement income, each can claim the credit, even though filing a joint return. If both are 65 or over and file a joint return, they may use an optional calculation which grants $2,286 as maximum retirement income instead of the standard $1,524.

Eligible Retirement Income

- Eligible retirement income for taxpayers under 65 includes only pensions and annuities under public retirement systems. Eligible retirement income for taxpayers 65 and over includes all pensions and annuities, as well as interest, dividends, and gross rents.

- Eligible retirement income must be reduced by amounts received under Social Security and the Railroad Retirement Act regardless of age of taxpayer. Taxpayers 72 and over make no further reductions. Taxpayers 62 but under 72 must further reduce the eligible retirement income by a portion of earned income received over $1,200 (one-half of the amount between $1,200 and $1,700 and all of the rest). taxpayers under 62 must further reduce eligible retirement income by all earned income received over $900.

- Earned income includes all wages, salaries, and professional fees received. For taxpayers engaged in a trade or business, such as farming, where both capital and the taxpayer's personal services are income producing factors, a reasonable amount (not over 30 percent) of net profit is considered earned income.
Who Will Likely Benefit?

Farmers most likely to benefit from the retirement income credit are those over 65 years of age in the following situations:

- Those who still own a farm but who have rented it to another operator.

- Those who have sold their farm and receive significant sums in interest or dividends.

- Those who are still operating their farms, but who have slowed down to the point where net farm profits are low, and who receive significant sums in interest, dividends, or rents from other sources.

Few farmers receive income from retirement systems other than Social Security. For this reason, it is rare to find a farmer under age 65 who will benefit from the retirement income credit.

Farm wives who have worked off the farm often receive income from retirement systems. These should not be overlooked by the farm family when filing their tax returns.

Farmers over 65 who continue to operate large and profitable farm businesses are also unlikely to benefit because their income is derived largely from the farm itself, none of which qualifies for the credit and some of which will be classified as earned income and thus reduce or eliminate any eligible income from other sources.

Farmers 65 or over should have a general understanding of the retirement income credit provisions of the Federal Income Tax Law. Some will find that they have been failing to claim credit for which they are eligible. Others will be influenced in their plans to discontinue active farming or to change their farming activities.

When both spouses are 65 years of age or older and file a joint return, they should compute their Retirement Income Credit under the General Rule as well as under the Alternative Computation. They can then compare the results and choose the method which will result in the greater credit.
Retirement Income Credit

Example - Harry and Wilma Grant are both 66 years of age and file a joint return for 1969. Harry meets the 10 year prior earned income test but Wilma does not. Harry received in 1969 a taxable pension of $5,000 from his former employer, wages of $1,400 from part-time work, and a Social Security pension of $1,000. Wilma received Social Security benefits of $500 and wages of $1,300. The retirement income upon which the credit is based is determined as follows:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total combined retirement income</td>
<td>$5,000</td>
</tr>
<tr>
<td>Maximum amount upon which the credit may be based</td>
<td>$2,286</td>
</tr>
<tr>
<td>Harry's Social Security pension</td>
<td>$1,000</td>
</tr>
<tr>
<td>Wilma's Social Security pension</td>
<td>500</td>
</tr>
<tr>
<td>One-half of Harry's wages over $1,200 but not over $1,700</td>
<td>100</td>
</tr>
<tr>
<td>One-half of Wilma's wages over $1,200 but not over $1,700</td>
<td>50</td>
</tr>
<tr>
<td>Retirement income upon which the credit is based</td>
<td>$636</td>
</tr>
</tbody>
</table>

Therefore, their joint retirement income credit for 1969 under the alternative computation is 15 percent of $636 or $95.40.

If the alternative computation were not elected, Harry's retirement income credit would be determined as follows:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Maximum amount upon which credit may be based</td>
<td>$1,524</td>
</tr>
<tr>
<td>Harry's Social Security pension</td>
<td>$1,000</td>
</tr>
<tr>
<td>One-half of Harry's wages over $1,200 but under $1,700</td>
<td>100</td>
</tr>
<tr>
<td>$424 x 15% = $63.60</td>
<td></td>
</tr>
</tbody>
</table>

Wilma would have no retirement income credit as she did not meet the 10 year prior earnings test. Therefore, by electing the special provision, the taxpayers will receive a tax saving of $31.80 ($95.40 minus $63.60).

Reporting Calculations

Calculations for the retirement income credit are made on Form 1040R.
Starting in 1968, self-employed persons including farmers can shift part of their income to their retirement years by investing in qualified retirement programs. Liberalized provisions of the Self-Employed Individuals Tax Retirement Act of 1962 (Keough Act) make it possible and practical for farmers and other self-employed persons to set up a retirement program for themselves and their regular employees on a tax sheltered basis.

For a consistently profitable farm business, this kind of retirement planning can also be good tax management. A retirement plan can help to create a sound basis for income in later years for both the farmer and his regular employees. It can help to minimize income taxes by postponement of tax obligation to retirement years when total taxable income is likely to be less.

Contributions

Starting in 1968, owner-employees may contribute up to 10 percent of their earned income to a maximum of $2,500 to a qualified retirement plan. In 1967 and before, only half of these amounts were deductible.

All full-time employees with three or more years of consecutive service must be included in the retirement program. Employees with less than three years service may also be included. Deposits made by the owner-employee for his employee are tax deductible for the owner-employee but are not taxable to the employee until he gets the distribution during his retirement.

Owner-employees decide each year if they wish to contribute to the fund. They need not contribute each year. However, if the plan includes employees, the contribution must be made for them as required by the plan.

The owner-employee may deduct his contributions and those made on behalf of his employees and still itemize non-business deductions, take the standard deduction, or the minimum standard deduction. Contributions for farm employees are entered as a farm expense on 1040F.
Investment Alternatives

The funds may be held or invested in several ways. Many investment companies, banks, trust companies, and insurance companies have plans for investment of these retirement funds which are designed especially to meet the requirements of the Self-Employed Individuals Tax Retirement Act. These include:

a) Purchase of nontransferable annuity or endowment contracts

b) Purchase of special U.S. Retirement Bonds

c) Purchase of "face amount investment certificates" either nontransferable or held by a trust

d) Purchase of mutual fund or investment stock shares to be held by a bank as custodian

e) Contributions to a trust or custodial bank account

All qualified plans prohibit the payment of any benefits prior to age 59 1/2 years except in the case of death or disability. Distribution must have commenced by age 70 1/2 for owner-employees and for other employees at age 70 1/2 or at retirement, whichever is later.

A farmer can set up his own retirement system if he obtains approval from the Internal Revenue Service. However, in most cases, it is more practical to choose one of the plans provided by a well-established firm in the area.

It is possible to discontinue a retirement plan, but there are costs to the farmer if he drops the plan. For this reason, a farmer should give this question careful consideration before deciding to go into a plan.

A farmer who decides that he may be interested in entering into a self-employed retirement plan should seek competent counsel. Attorneys, bankers, tax consultants, investment counselors, and insurance representatives can be helpful in choosing a suitable plan which will satisfy requirements of the Internal Revenue Service.
FEDERAL INCOME TAX
SUGGESTIONS FOR PART-TIME FARMERS AND COUNTRY DWELLERS

People who work in town and live in the country sometimes derive income from their rural holdings. This income may be in the form of land or barn rent from a neighboring farmer, in the form of Government payments, from the sale of farm products, or other farm income. The manner in which such income and associated expenses should be reported to Internal Revenue depends on the kind and amounts involved. The following questions and answers may help to clarify the Federal income tax responsibilities of nonfarmers who have some farm income.

1. **Who is a farmer?** For tax purposes, if you receive at least two-thirds of your gross income from "farming" you are a farmer. Farmers use Federal Form 1040, Schedule F, to calculate their net earnings for tax purposes. Farmers must pay their tax by February 15.

2. **What is hobby farming?** If a farm is operated for recreation or pleasure, and the expenses are in excess of receipts, the expenses are regarded as non-deductible **personal** expenses, and the receipts may be omitted from gross income. If receipts exceed expenses, however, the excess must always be included in income. If the taxpayer can show that he is attempting to show a profit, his farm operations will generally not be classified as a hobby farm. If losses reported exceed $50,000 for five consecutive years, the operations will definitely be classified as hobby farming, and expenses disallowed.

3. **How do nonfarmers report income from farming?** Any non-farmer may use Federal Form 1040, Schedule F to report income and expenses related to farming, regardless of the amount. However, small amounts of both income and expense can be reported on 1040R as "other income." It is suggested (this is only a rule of thumb) that if farm income is from more than one source or exceeds $500, a farm Schedule 1040F be completed and filed with the Federal return Form 1040.

4. **What about quarterly estimates?** Farmers are not required to file quarterly estimates because they file their returns by February 15 instead of April 15. If your major source of income is wages or salary subject to withholding, but you receive some income in addition from farming, or other sources, you probably should file quarterly estimates. Generally, all taxpayers who receive enough outside income to require payment of $40 or more in tax in addition to tax withheld, must file the quarterly estimates.

5. **Can a part-time farmer take depreciation?** If you can show that you are attempting to make a profit on your farming, you can offset income with all appropriate expenses, including depreciation. For example, if you are renting out your barn, you can take depreciation on your investment in the barn. If you are renting land, you can depreciate your investment in tile drains and fences. You cannot depreciate land.

6. **What about income from wood, timber, or Christmas trees?** Small amounts of income from these sources may be reported on the farm Schedule 1040F. You are allowed to recover your original investment in trees as a depletion allowance on Schedule F. For larger amounts of income from sale of wood, timber, and Christmas trees, it may be possible to use Schedule D and receive gains treatment on at least a portion of such income.
7. Can a part-time farmer earn Social Security benefits from farm income? If you had net earnings of $400 or more from farming and less than $7,000 in wages, you must pay Social Security tax on the farm earnings. If you had less than $400 net from farming, but at least $500 gross income from farming, you may get Social Security credit from farm income if you want. Use Form 1040SE to calculate and pay the self-employment tax.

8. Where should income from rural recreation facilities be reported? A farmer or a non-farmer with minor income from renting campsites, boats, etc., may report this income on 1040S as "other income." If such income is substantial, Schedule C, Form 1040, should be filed and the recreation facilities thus reported as a separate business.

9. What Federal tax schedules should be used to report income to part-time farmers and country dwellers? The following table lists common items of income to part-time farmers, and forms which may be used to report this income.

<table>
<thead>
<tr>
<th>Source</th>
<th>Form to Use</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rent of land or buildings</td>
<td>Schedule E, Form 1040</td>
</tr>
<tr>
<td>Rent of house</td>
<td>Schedule E</td>
</tr>
<tr>
<td>Interest and dividends</td>
<td>Schedule F, Form 1040</td>
</tr>
<tr>
<td>Sale of wood, lumber, or Christmas trees</td>
<td>Schedule F, Form 1040, for small amounts. Schedule D for larger amounts.</td>
</tr>
<tr>
<td>Sale of fruit, berries, garden produce</td>
<td>Schedule F</td>
</tr>
<tr>
<td>Sale of honey or maple products</td>
<td>Schedule F</td>
</tr>
<tr>
<td>Sale of standing hay</td>
<td>Schedule F</td>
</tr>
<tr>
<td>Tractor or machine work for neighbors</td>
<td>Schedule F</td>
</tr>
<tr>
<td>Sale of eggs and chickens</td>
<td>Schedule F</td>
</tr>
<tr>
<td>Sale of livestock held for sale</td>
<td>Schedule F</td>
</tr>
<tr>
<td>Income from Government farm programs</td>
<td>Schedule F</td>
</tr>
<tr>
<td>Soil and gravel sales</td>
<td>Schedule F</td>
</tr>
<tr>
<td>Nursery stock, flowers and plants</td>
<td>Schedule F</td>
</tr>
<tr>
<td>Sale of livestock held for dairy or breeding purposes</td>
<td>Schedule D, Form 1040</td>
</tr>
<tr>
<td>Sale of house lot or other land</td>
<td>Schedule D, Form 1040</td>
</tr>
<tr>
<td>Wages from occasional farm work</td>
<td>Form 1040</td>
</tr>
</tbody>
</table>

Small amounts of income from almost any source may be reported on Schedule E, 1040. For a business other than a farm, use Schedule C, Form 1040. Income from all sources must be combined on Form 1040 to calculate the tax due.
NEW YORK STATE INVESTMENT CREDIT

The 1969 session of the New York State Legislature passed an amendment to the State Tax Law, which provides for an investment credit for state tax purposes. The law will be effective for the 1969 income tax returns of farmers and for the returns of subsequent years.

Qualified Investments

Investments in new or used buildings, equipment, and other facilities used for production purposes qualify. The buildings or equipment must have been acquired, constructed, or reconstructed after December 31, 1968. Buildings may include storages for materials to be used in production or storages for products that are produced. Machinery, equipment, and facilities used in production, and equipment used in repair and service of other machinery all qualify.

Items must have a useful life of four years or more to qualify. The years used for the depreciation on the federal income tax return shall be considered to be the useful life. Property must be located in New York State to qualify. Investments may be made by individuals, unincorporated businesses, or by corporations. Property that is leased to others does not qualify.

Calculation of Credit

The amount of the credit is one percent (1%) of the cost or other basis for federal income tax purposes of the qualified investment. A new Form IT212, with instructions, will be used to calculate the credit.

Use of the Credit

The investment credit can be used to reduce the state personal income tax, the franchise tax, or the unincorporated business tax. If the amount of the credit allowable exceeds the taxpayer's tax for such year, the excess may be carried over and deducted from the taxpayer's tax of the following year or years.

Disposition of Qualified Property

For property which is disposed of or ceases to be used for qualified purposes during the taxable year in which the credit is to be taken, the allowable credit shall be the proportion represented by the ratio of the months used to the total useful life of the property.

For property that is disposed of or ceases to be in qualified use prior to the end of the useful life, the difference between the credit taken and the credit allowed for actual time in use must be added back in the year of disposition. If property disposed of has been in use 12 or more consecutive years, it shall not be necessary to add back any credit.

New York vs. Federal Investment Credit

The New York investment credit differs from the federal investment credit in that (1) it includes buildings, (2) it is limited to facilities used in production, (3) the years used for depreciation are the useful life, and (4) the rate is one percent.
QUESTIONS AND ANSWERS ON THE NEW YORK STATE PERSONAL INCOME TAX

The new State Income Tax Law now conforms closely with the Federal Internal Revenue Code.

Farmers must compute their Federal income tax, then carry the adjusted gross income over to the appropriate State form. There is no New York State farm tax form.

New York adjusted gross income is the basis for computing the New York personal income tax and with few exceptions is the same as Federal adjusted gross income.

It is not necessary to compute capital gains and losses separately in arriving at New York adjusted gross income because all capital gains and capital losses are automatically included in New York adjusted gross income to the same extent they are for Federal income tax.

Questions and Answers about New York Returns

1. Who must file a New York State income tax return; when is it due?

   Every New York resident who is required to file a Federal income tax return for the taxable year must file a New York State income tax return. It will also be necessary to file a return if a tax refund is being claimed, even though the individual is not otherwise required to file a return. The New York State return is due at the same time the Federal return is due.

2. Who must file a New York Declaration of Estimated Income Tax?

   A declaration must be filed by every taxpayer (except farmers) whose total New York income from sources other than wages is expected to exceed $600 times the number of his exemptions, plus $400.

3. Are Farmers Required to File a Declaration of Estimated Income Tax?

   No. If two-thirds of total New York adjusted gross income is from farming, no estimate is required for either New York personal income tax or for New York unincorporated business tax. Farmers' filing dates for both are the same as for Federal income tax.

4. What is New York adjusted gross income?

   New York adjusted gross income is computed by starting with Federal adjusted gross income and adding or subtracting some income items which were exempt from Federal tax but not from State tax, or vice versa.

5. What items must be added to Federal adjusted gross income to arrive at New York adjusted gross income?

   The following are the most common items which must be ADDED to Federal adjusted gross income:

   A. Interest on bonds of states or localities other than New York, the income from which is exempt from Federal income tax.
B. Interest or dividend income on bonds or securities of any U. S. authority exempt from federal tax but not from state income tax.

C. Any income tax deducted as a business expense or otherwise in computing Federal adjusted gross income. (New York State unincorporated business tax)

6. What items may be subtracted from Federal adjusted gross income to arrive at New York State adjusted gross income?

The following are the most common items which may be SUBTRACTED from Federal adjusted gross income:

A. Any interest on United States bonds which was included in the taxpayer's Federal adjusted gross income.

B. Any pension received by a retired officer or employee of New York State or its cities, etc., which was included in the taxpayer's Federal adjusted gross income. This applies to pensions paid by New York State and related retirement systems.

C. A refund of income tax from New York State or any other taxing authority if the refund was included in Federal adjusted gross income.

D. A portion of any gain from sale of property included in Federal adjusted gross income if the property had a higher adjusted basis on December 31, 1959 for New York State income tax purposes than for Federal income tax purposes. The amount which may be subtracted is the difference in basis. (If the gain is considered a long-term capital gain for Federal income tax purposes, the amount is limited to 50 per cent of the difference in basis.)

<table>
<thead>
<tr>
<th>Description</th>
<th>Federal</th>
<th>State</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tractor bought January 1, 1958</td>
<td>$3,500</td>
<td>$3,500</td>
</tr>
<tr>
<td>Depreciation allowed</td>
<td>-1,260</td>
<td>-760</td>
</tr>
<tr>
<td>Adjusted basis December 31, 1959</td>
<td>$2,240</td>
<td>$2,740</td>
</tr>
</tbody>
</table>

Amount State basis exceeds Federal $560

7. How are these additions and subtractions made when a husband and wife file a joint Federal income tax return but elect to file separate New York State income tax returns?

The husband and wife must each first determine his or her own separate Federal adjusted gross income as if separate Federal returns had been filed. Then each must make the necessary additions or subtractions to his or her own Federal adjusted gross income. To compute their tax on such a separate basis, a husband and wife will use a single form (IT 206) which is included in the resident packet IT 201 P.
8. May a taxpayer use different methods of computing depreciation for Federal and New York income tax purposes if he was using different methods prior to 1960?

   No. Since the computation of New York adjusted gross income starts with Federal adjusted gross income, the same depreciation deduction allowed for Federal income tax purposes must be used for New York income tax purposes.

9. Is it necessary to compute separately capital gains and losses in arriving at New York adjusted gross income?

   No. All capital gains and capital losses automatically are included in New York adjusted gross income to the same extent they are for Federal income tax purposes. Note: For New York unincorporated business tax income, capital gains are included at 100 per cent.

10. How does the tax investment credit affect the New York State income tax return?

    The State does not recognize the investment credit feature of the Federal tax structure. No calculations, adjustments, or entries are to be made on the State returns relative to investment credit. (See p. 34)

11. If a husband and wife each have separate income, and filed a joint return for Federal, is it an advantage to file a New York combined income tax return?

    If they both have separate income, they should compute their tax on the resident return IT 201 and on the combined form IT 208, and use the return that is most advantageous. Sometimes the combined form will result in a lower tax because more of the income is taxed in lower brackets.

12. What deductions are allowed for New York income tax purposes?

    A standard deduction of 10 per cent of New York adjusted gross income, which may not exceed $1,000, is allowed to every taxpayer not claiming the New York itemized deduction.

13. Is the New York standard deduction of a husband and wife computed the same as for an individual taxpayer?

    Yes, if they file a joint New York return. But if they file separate New York returns, the total standard deduction for both is limited to $1,000 or 10 per cent of their combined New York adjusted gross incomes, whichever is less.

14. Is the standard deduction of a husband and wife filing separate New York returns the same as their Federal standard deduction?

    No. It is based on New York adjusted gross income and may be divided between the two returns in any manner. (The Federal standard deduction of a married person filing a separate return is limited to $500.)
15. Must a taxpayer use the standard deduction for New York income tax purposes?

Only if he used the standard deduction for Federal income tax purposes. If he itemized his deductions for Federal income tax purposes, he may elect either to take the standard deduction or itemize his deductions for New York income tax purposes.

16. What additional deduction may an individual add to his Federal itemized deductions to arrive at the amount of the New York itemized deduction?

Up to $150 for life insurance or endowment policy premiums, net after dividends, upon the life of the taxpayer. If a husband and wife file a joint New York return, a deduction may be claimed for such premiums up to $150 actually paid on each one's life.

17. If a husband and wife file a joint Federal income tax return but file separate New York State income tax returns on the combined form IT 208, what exemptions are allowed?

The husband and wife are each allowed a New York exemption of $600 for each Federal exemption to which he or she would have been entitled if separate Federal returns had been filed.

18. Is income tax paid to New York State deductible on the Federal return?

The State income tax and, except in the case of a partnership, the State unincorporated business tax, are not deductible on Federal Schedule F as business expenses. They are deductible on Schedule 1040 if deductions are itemized. The unincorporated business tax is not deductible because it is a tax on net income instead of gross income and is therefore considered a personal rather than business expense (see Federal Tax Guide for Small Businesses).
QUESTIONS AND ANSWERS ON THE NEW YORK STATE UNINCORPORATED BUSINESS TAX

1. What is the unincorporated business tax and what farmers must file?

   This is a tax, in addition to the income tax, levied on the net income of unincorporated businesses, including farm businesses operated by individuals or by partnerships.
   Every farmer or farm partnership with a gross income of more than $10,000 from the farm business must file. It is possible, but highly unlikely, that a farmer with less than $10,000 gross could have over $6,250 net and thus be required to file a return.

2. What income is considered in calculating unincorporated business tax?

   For a farmer on a cash basis it includes:
   A. Net farm income from page 1 of Federal Schedule F; plus:
   B. All the gain from sale or exchange of real or personal property (including livestock held for draft, breeding or dairy purposes) carried as business assets (except real property held outside New York State).
   C. Plus other business income.

3. What form is used and what is the filing date for the unincorporated business tax?

   Form IT 202 for the individual. Form IT 204 for partnerships.
   The filing date is February 15, the same date personal income tax is payable. It should be attached to the personal income tax return.

4. Is there any allowance for taxpayer's services or personal exemption?

   Yes. Up to 20 per cent of the total net income from the business or $5,000, whichever is lower, is allowed for the personal services of the taxpayer. In addition there is a flat statutory exemption of $5,000 (if business was conducted for a full 12 months).

5. What credit toward the unincorporated business tax can be taken after the tax is computed?

   An amendment to the unincorporated business tax law includes a provision for a credit for the entire amount of the tax, if the tax is $100 or less and a graduated reduction of the tax if it is between $100 and $200.

6. How are capital gains and losses treated for the unincorporated business tax?

   Capital gains and losses from the sale or exchange of stocks, bonds, or real estate carried as business assets are fully taxable and deductible, respectively.

7. May a loss from operating a farm business be carried forward to offset future income subject to the unincorporated business tax?

   No.

8. Suppose a man has two or more unincorporated businesses, does he file separate returns for each business?

   No. The operations of the businesses must be consolidated.
FARM TAX TIPS

1. Note the changes made in the tax forms for 1969. Form 1040 is now a single page. Many farmers will be using the new Schedules A and B. All farmers will use the new Schedule SE and Schedule T.

2. Form 4255 is new and should be used for computing the "Recapture Tax" from a prior year's investment credit.

3. Form 1040-X, which was new in 1968, may be used to correct an individual income tax return for any year. For example, a farmer who neglected to claim investment credit last year, may file 1040-X with Form 3468 attached to claim the credit.

4. The tax surcharge which became effective April 1, 1968 increases your normal 1969 income tax by 10 percent (it may be less if the normal tax is less than $735).

5. Investment credit represents an important federal income tax saving for most farmers. A dollar of investment credit is equivalent to several dollars of depreciation.

6. Operators of profitable farm businesses should investigate possible advantages of setting up a qualified retirement pension plan for themselves and their regular employees.

7. Some older farmers can reduce their income tax by using retirement income credit as computed on Schedule R (Form 1040).

8. Gasoline tax credit used to reduce income tax must also be reported as income. Such credit used by a cash basis taxpayer to reduce 1969 tax becomes income in 1970. Be sure to enter your 1968 credit on your 1969 return.

9. A farmer may deduct as a labor expense, reasonable cash wages paid his child for work actually performed by him.

10. Most farm business record books and electronic farm business accounting systems provide an acceptable classification of farm expenses for use in Part II of Schedule F. Under "Other (specify)" write in classes of expenses used in your records but not listed in Part II.

11. Many expenses are part personal and part business. These must be allocated for income tax purposes. Common examples of such expenses are real estate taxes, fire insurance, electricity, telephone, auto expenses, gas and oil, and travel expenses.

12. In computing net earnings from self-employment, you must claim all allowable deductions including depreciation.

13. Most farmers in years of low earnings will benefit by electing the optional method provided in Part II of Schedule SE for computation of net earnings from farm self-employment. This provides a better base for Social Security benefits upon retirement or in case of death.
14. Income from the sale of livestock held for dairy or breeding purposes should always be reported on Schedule D and never on Schedule F.

15. Depreciation allowances are lost if not taken in the year they are allowable. The special 20 percent first year depreciation is available only the first year depreciation is allowable.

16. Tax management should be aimed first at using all allowable exemptions and deductions each year.

17. Partnerships must use Form 1065 and Schedule D (Form 1065). Schedule F (Form 1040) is used to report farm partnership income and expenses. Only one Schedule F need be filed.

18. Money items on tax returns may be shown in whole dollars. To do this, eliminate amounts of less than 50 cents and increase amounts of 50 cents through 99 cents to the next highest dollar.

19. Agricultural employers must withhold Social Security tax from the wages of any employee who during the year earns $150 or more or who works 20 days or more for cash wages (except some family employees). Farmers are not permitted to withhold income tax from employees wages.

20. Farmers who employ help can save time in preparing reports by using optional Form W-2 for reporting wages paid farm employees.

21. Complete farm business records are essential for good income tax reporting. Incomplete records frequently result in paying more tax than is actually due.

22. The sale of a farm and other business assets frequently involves important tax considerations. A farmer needs competent professional advice in making arrangements for such a sale.

23. Investment credit is now available for New York State Income and Unincorporated Business Taxes. Do not overlook this tax credit.

24. If both husband and wife have incomes, it is usually advantageous to file separate state income tax returns even though a joint return is used for the federal tax.

25. Farmers can benefit by making contributions to their church or charity in the form of a crop or livestock.

26. Farmers with unusually good incomes for 1969 may find tax averaging to their advantage too.

27. Be sure to make a final check of all tax returns. Errors in arithmetic, missing Social Security numbers, and missing signatures are common errors.