

# Don't let the clock strike 12

Estimate 2011 (and 2012) taxes and make decisions before Dec. 31.



**T**ime is ticking on tax planning. Many producers who operate on the calendar year need to sharpen their pencils and make decisions by Dec. 31. If the clock strikes midnight before you act, some tax deductions can turn back into pumpkins.

The combination of good yields, strong markets and 2011 crop input expenses prepaid in 2010 is resulting in much larger tax liability than many producers expected. This income tax liability has producers contemplating various strategies, but a “good” plan is a combination of tax and business management.

### Tax management, not avoidance

Review the tax brackets for future and past years. Consider your

projected income in the future. If you know you'll be in the 25 percent tax bracket next year, make sure you fill up the 15 percent bracket this year. For past years, make sure you have filled up the previous year's lower tax brackets — if not, consider income averaging (discussed below).

Consider tax deductions and/or credit limits and phase-outs: Deductions are items “deducted” from your income — standard deductions (or itemized) and personal exemptions. Be sure to review these amounts when calculating your taxable income. Credits are a dollar-for-dollar reduction in tax liability such as child care, earned income or energy that can be refundable or non-refundable (limited to your tax liability).



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



Some deductions and/or credits have a set “maximum” amount based on IRS regulations, your adjusted gross income, earned income, etc.

### Does the glass slipper fit?

Consider how your decisions will impact your profitability and cash flow. Just because a capital purchase will decrease your tax liability doesn't necessarily make it a good management decision. Always consider the cash flow needed in future years: You'll be paying these principal payments with “after-tax” dollars.

### Other considerations

Other people may use your tax return information as a source document. You also may want to consider:

- Social Security earning limits
- College financial aid limits

By considering all the variables, you can decide on an “ideal” income level to use for tax planning.

Options to adjust taxable income for cash-basis producers are:

- **Prepay operating inputs.** Be sure to specify a quantity and price. Remember, prepaid expenses are limited to 50 percent of deductible expenses.
- **Defer crop insurance proceeds.** You may elect to defer income to the following year if you normally sell in the following year.
- **Pay your children a reasonable wage for farm work.** You don't have to pay Social Security tax on your children under age 18. You must file the appropriate payroll tax forms.
- **Pay any accrued interest.**
- **Consider income averaging.** Depending on the prior year's taxable income, income averaging may decrease your tax liability.
- **Double up on church or charity contributions.** If you itemize, consider donating more or paying state income tax in December instead of waiting until the following year.
- **Review Commodity Credit Corporation (CCC) loan tax treatment.** If you have “sealed grain” carrying over at year-end, simply electing to change the tax treatment may increase or decrease your taxable income. You may need to file additional forms with your return.
- **Capital assets.** Be your own fairy godmother: Consider purchasing needed capital assets such as equipment, buildings or breeding livestock. The federal depreciation rules are described below; however, each state decides if they'll couple or decouple from these. Check on the depreciation rules for your state.
- **Bonus depreciation for purchased capital assets.** An additional first-year depreciation deduction equal to 100 percent of adjusted basis for qualified property is available for both regular income and alternative minimum tax

(AMT). A general description for qualified property is:

- MACRs (Modified Accelerate Cost Recovery) property with 20 years or less recovery period.
- Original use required by taxpayer (new).
- Property must be placed in service before Jan. 1, 2012.
- **Utilize the “quick write-off” depreciation for purchased capital assets.** For 2011, the Section 179 deduction is \$500,000. The 179 election is limited to qualified capital purchases for items such as equipment, grain bins or breeding livestock with a dollar-for-dollar phase-out starting at \$2 million. Additionally, qualified items that exceed the \$500,000 are eligible for regular depreciation.
- **Fund your retirement account — IRA, SEP, Keogh.** Because some plans need to be set up by Dec. 31, be sure to check into this now. The limits for 2011 for the traditional deductible retirement accounts are:
  - **Traditional IRA.** These are available to any individual under the age of 70½ with earned income. For 2011, the maximum contribution is \$5,000 or your earned income (whichever is less). Individuals age 50 or older also can make an additional \$1,000 “catch up” contribution. This increases the limit to \$6,000. However, be aware of income phase-out limits. These phase-out limits differ depending on filing status (married filing joint, head of household, single, etc.) and the type of IRA (traditional or spousal). For example, if you are married, filing a joint return and were eligible to participate in an employer-sponsored plan such as a 401k, the IRA contribution drops when your income exceeds \$90,000.
  - **SEP/Keogh.** These retirement plans may permit greater contributions and deductions. However, you generally will run into provisions requiring contributions for other employees who meet certain minimum qualifications. The deduction is limited to percent of net self-employed income minus the self-employment tax deduction for the self-employed individual or a percent of wages for an employee. The maximum level is 20 percent for a self-employed individual and 25 percent of wages for an eligible employee with a maximum limit of \$49,000. However, certain already-established plans may have different contribution percentages and limits. See the IRS publication 560 for complete details.

These are some of the most common strategies. We must emphasize making your tax estimate before the clock strikes 12 on Dec. 31. Because of tax law changes and various sunset dates, it's vital to review your tax estimate with your tax consultant or financial adviser. An hour with a tax consultant before New Year's Eve can save thousands of dollars on your final tax return. 