

Income Tax Issues: Weather-Related Sales of Livestock

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Weather-Related Sales of Livestock

- **Special Income Tax reporting may be available for**
 - **Sales in excess of normal business practice**
 - **Caused by weather-related conditions**
 - **Drought**
 - **Flood**
 - **Other conditions causing a shortage of water and/or feed**
- **Special rules depend on**
 - **Whether market or breeding livestock**
 - **Whether disaster declaration issued**

Involuntary Conversion

Internal Revenue Code Sec. 1033(e)

- **Applies to breeding, dairy or draft livestock**
 - No holding period requirement
 - Does not apply to livestock held in the ordinary course of trade or business (Market Livestock)
- **Held for Breeding**
 - Animal determined to be “held for breeding” when selected for addition to breeding herd
 - Raised Animals – Selection made when animals selected to remain on farm for addition to breeding pool, rather than for sale as market livestock
 - Purchased Animals – Selection generally made when animal is purchased and brought to farm
 - Animals purchased before reaching useful age???

I.R.C. Sec. 1033(e) Rules

- Reporting gain postponed by purchasing replacement animals
 - Replacement period runs 2 years from end of sale tax year
 - No federal disaster declaration needed
- Special Rules
 - Replacement period is 4 years if weather conditions lead to federal disaster declaration
 - Replacement period can be further extended by IRS in cases of on-going drought
 - Replacements must be like use
 - If sale conditions also make like use replacement impossible, replacement can be made with any property
 - No disaster declaration required to replace with unlike property if like-use replacement prevented

Understanding Deferral of Gain

- Deferral of gain based on sale \$ per head
- If 10 animals sold at \$600/hd, then at least 10 animals must be repurchased at at least \$600/hd
 - If 9 animals repurchased at \$700/hd, \$600 sale of animal not replaced must be reported on amended return
 - If 12 animals repurchased at \$550/hd, \$500 of gain (10 hd x \$50) must be reported on amended return for the 10 replacement animals repurchased below original animals' sale price

Sec. 1033(e) Special Rules

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1 Year Deferral of Income

- Election made under Internal Revenue Code Sec. 451(e)
- Applies to all livestock (market and breeding, dairy, draft)
- Taxpayer
 - Principal business must be farming
 - Must use cash method of accounting
- Weather-related conditions must also cause federal disaster declaration

Making an Election

- **Internal Revenue Code Sec. 451(e)**
 - Election must be made by due date of return, including extensions, for the sale year
 - Election can be revoked, but cannot be made on an amended return
- **Internal Revenue Code Sec. 1033(e)**
 - Election can be made any time during replacement period (2 years, or 4 years)
 - If election revoked, gain must be reported in year of sale

Animals Eligible for Either Election

- **Animals (breeding, dairy, draft) eligible for either election (Federal disaster declaration)**
- **Special rules permit revocation of Sec. 1033(e) election and adoption of Sec. 451(e) election during 4-year replacement period**
 - **Allows election of one-year reporting deferral (reporting in year following sale year) on amended return**
 - **Permits avoidance of reporting in sale year if Sec. 1033 (e) election made, and replacement subsequently deemed impractical**