



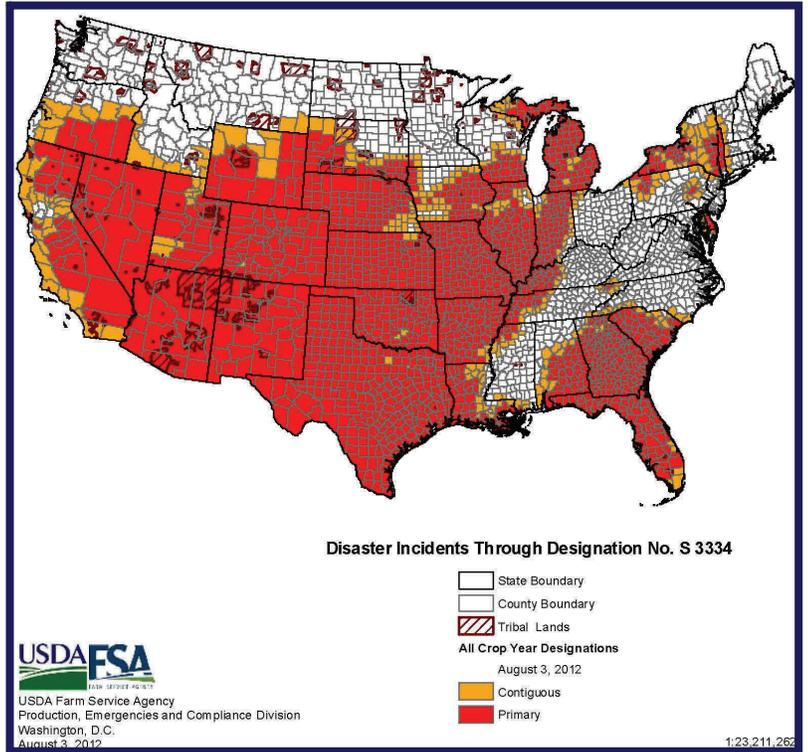
# Drought Assistance

## Drought Assistance Overview

To respond to immediate needs of farmers and ranchers struggling with the impact of one of the worst droughts in decades, the U.S. Department of Agriculture (USDA) and other federal agencies are using existing authorities wherever possible to address the hardships arising from the lack of water, feed and forage. Within the last month, USDA has opened the Conservation Reserve Program (CRP) to emergency haying and grazing, lowered the borrower interest rate for emergency loans and called on crop insurance companies to provide more flexibility to farmers.

Below is an overview that you may find helpful.

- ◆ According to the USDA, roughly 70 percent of cattle producing regions are suffering from drought conditions.
- ◆ More than half (50.3 percent) of all counties in the United States have been designated disaster areas by USDA in 2012, mainly due to drought.



## Livestock Assistance

Click on red underlined links for websites with additional information.

### Emergency Conservation Program

Provides emergency funding and technical assistance for farmers and ranchers to rehabilitate farmland damaged by natural disasters and for carrying out emergency water conservation measures in periods of severe drought.



Contact local FSA office for additional information.

### Emergency Haying & Grazing

Emergency haying and grazing of CRP acreage may be authorized to provide relief to livestock producers in areas affected by a severe drought or similar natural disaster.



Authorization is provided by either a national FSA office authorization or by a state FSA committee determination utilizing the U.S. Drought Monitor.

### EQIP Modifications

Provides financial assistance to help plan and implement conservation practices. Modification of current EQIP contracts to allow conservation activities to address drought conditions.



Information about how to apply for assistance through EQIP is available online.

# Loan Assistance

## Wetland Reserve Program

USDA is authorizing haying and grazing of WRP easement areas in drought-affected areas where such haying and grazing is consistent with conservation of wildlife habitat and wetlands.



Contact [local NRCS office](#) for additional information.

## Emergency Loans

USDA's Farm Service Agency (FSA) provides emergency loans to help producers who own or operate located in a county declared by the President or designated by the Secretary of Agriculture as a primary disaster area or quarantine area. All counties contiguous to the declared, designated, or quarantined primary counties also are eligible for emergency loans. The maximum loan amount for an emergency loan is \$500,000.

### **Emergency loan funds may be used to:**

- ◆ Restore or replace essential property
- ◆ Pay all or part of production costs associated with the disaster year
- ◆ Pay essential family living expenses
- ◆ Reorganize the farming operation
- ◆ Refinance certain debts, excluding real estate

## Emergency Debt-Set-Aside Program

When FSA borrowers located in designated disaster areas or contiguous (adjoining) counties are unable to make their scheduled payment on any FSA debt, FSA is authorized to consider set-aside of one payment to allow the operation to continue.

When the county in which a borrower farms, or a contiguous county, is designated as a disaster area by the president or secretary of agriculture, farmers presently indebted to FSA will be notified of the availability of the Disaster Set-Aside Program.

## Guaranteed Loan Program

Guaranteed Operating Loans (OL) may be used to purchase livestock, farm equipment, feed, seed, fuel, farm chemicals, insurance, and other operating expenses. Operating Loans can also be used to pay for minor improvements to buildings, costs associated with land and water development, family living expenses, and to refinance debts under certain conditions.

Click on [red underlined](#) links for websites with additional information.

## **Resources**

- ◆ USDA Drought and Disaster Assistance: [Website](#)
- ◆ Find your local Farm Service Agency (FSA): [Map](#)
- ◆ Emergency Disaster Designation and Declaration Process Overview: [Fact-sheet](#)
- ◆ Disaster Designated Counties: [Map](#), [List of Counties](#)

## Tax Options

If a producer is forced to sell livestock, in excess of normal levels, due to shortages of water, feed or other consequences of drought, the income tax on the gain from the sale of those animals may be postponed.<sup>(1)</sup> Producers have two distinct options tax options available to them in this circumstance:

1. **Code Section 451(e):** The election to postpone reporting the taxable gain on the additional sales of any livestock for one year <sup>(2)</sup>; or
2. **Code Section 1033(e):** The election to postpone, and altogether avoid, paying taxes on the gain from the sale of breeding, draft, or dairy animals if they are replaced within a specified time frame.<sup>(3)</sup>

### Summary of Tax Options for Drought Sales of Livestock

Question	Section 451(e)	Section 1033(e)
What livestock qualifies?	All livestock.	Breeding, draft, or dairy livestock
Must the county be eligible for federal disaster assistance?	Yes	No, but declaration increases replacement period to 4 years
Must livestock be sold in affected area?	No	No
What sales does the election apply to?	Sales in excess of normal business practices.	Sales in excess of normal business practices.
Must weather have caused the sale?	Yes	Yes
How does the election benefit me?	Postponing payment of income taxes on the sale for one year.	Deferral of paying capital gains by carrying over basis, reinvestment timeframe applies.
Is replacement of the animals required?	No	Yes
What effects does the election have on basis?	N/A	Reduced by gain that is deferred
How long do I have to replace?	N/A	Two years from the end of the taxable year of sale or 4 years if area is eligible for disaster assistance
How long do I have to make the election?	Due date for return for year or sale for livestock held for resale and 4 years after the year of sale for draft, dairy, or breeding livestock.	Two years from the end of the taxable year of the sale

\* [Oklahoma Cooperative Extension Service](#) <sup>(4)</sup>

## Frequently Asked Questions About Code Section 451(e)

**Code Section 451(e):** Provides for the one year postponement of gain on the sale of all classes of livestock.

### Q: What requirements must I meet as a producer?

A: In order to qualify for this election a producer must meet the following criteria:

- ◆ Their principal business must be farming.
- ◆ They must use the cash method of accounting.
- ◆ They can show that under usual business practices, they would not have sold or exchanged the additional animals this year except for the weather-related condition.
- ◆ The weather-related condition caused an area to be designated as eligible for assistance by the federal government.[\(5\)](#)

### Q: How do I make the election?

A: The 451(e) election must be made by the due date of the tax return for the tax year in which the sale occurred [\(4\)](#), and the following information should be attached to the statement:

- ◆ A declaration that the producer is taking an IRS Code Section 451(e) exemption.
- ◆ Evidence of the weather-related conditions that forced the sale of the animals.
- ◆ The number of animals sold under normal business practices during each of the past three years.
- ◆ The number of animals that would have been sold during the current tax year had the producer followed their normal business practices.
- ◆ Information verifying that the area was designated as eligible for federal disaster assistance, and that date at which that designation was received.
- ◆ Computations, consistent with IRS requirements, to show the amount of income that is being deferred until the next year.[\(4\)](#)

### Q: What if my county has not received a federal disaster declaration at this time?

A: In order for a producer to qualify for a 451(e) election, the area must have received a federal disaster declaration; however, it is not necessary that the sale of the livestock takes place after the declaration was received. The sale of the animals could have occurred prior to the area receiving a designation as eligible for federal disaster assistance, as long as the weather-related condition that caused the federal disaster designation was the same condition that forced sale of the livestock.[\(5\)](#)

### Q: What is an example of a situation where this election could be applied?

A: A cow/calf producer with 100 cows typically sells 25 of his calves after fall weaning while retaining the remaining 75 for back-grounding and sale the next Spring. This year, due to drought conditions, the producer has depleted feed stocks and is forced to sell all 100 calves immediately following weaning in the fall. This producer could postpone paying taxes on the gain from the sale of the additional 75 head until the next year.

Click on [red underlined](#) links for websites with additional information.

## **Frequently Asked Questions About Code Section 1033(e)**

**Code Section 1033(E):** Provides for the postponement of gain on the sale of breeding, draft, or dairy animals when the producer intends to replace them at a later time.

### **Q: What requirements must I meet as a producer?**

A: In order to qualify for this election a producer must meet the following criteria:

- ◆ Their principal business must be farming.(5)

### **Q: Is the 1033(e) election limited to cash-basis taxpayers?**

A: No, a Section 1033(e) exemption is available to all taxpayers whose principal business is farming (unlike under Section 451(e)).(5)

### **Q: How do I make the election?**

A: The election to defer the payment of capital gains on the forced sale of livestock is made by demonstrating the involuntary conversion of those animals. This can be done by attaching the following information to the tax return for the year in which the sale of the animals occurred:

- ◆ A statement that the producer is electing to postpone gain under Code Section 1033(e).
- ◆ Evidence of the existence of the drought conditions that forced the producer to sell their livestock, and if applicable the date of federal disaster designation for that area.
- ◆ The number and kind of livestock that were sold.
- ◆ The number and kind of livestock that would have been sold should the producer have followed their normal business practices.
- ◆ A computation, consistent with IRS requirements, of the income that is being postponed.(5)

### **Q: How long do I have to replace the animals before I will be forced to pay capital gains?**

A: Two different time frames can apply dependent upon the disaster declaration status of a producers' county.

- ◆ Two years if the area is not declared eligible for federal assistance.
- ◆ Four years if the area is declared eligible for federal assistance.(5)

### **Q: Do I have to reside in a county that has been designated as eligible to receive federal disaster assistance in order to qualify for a 1033(e) election?**

A: No. Although the reinvestment time frame is limited to two years, producers whose county did not receive a federal disaster designation can still qualify for a 1033(e) election. (5)

### **Q: How is the 'first drought-free year' determined?**

A: Under IRS Notice 2006-82 the replacement period was altered to extend until the end of the first taxable year ending after the first drought-free year for the applicable region. A 'drought-free year' is defined as a year in which the producers area, meaning their county or any county contiguous, does not experience a severe, extreme, or exceptional drought for any weekly period between September 1st and the following August 31st.

Furthermore, determinations regarding the severity of the drought will be based upon the U.S. Drought Monitor (i.e.: D2: severe, D3: extreme, D4: exceptional).(6)

## Continued, Frequently Asked Questions About Code Section 1033(e)

### **Q: How will I know if a severe, extreme, or exceptional drought was reported for my area?**

A: Upon a visual evaluation of the U.S. Drought Monitor many producers will likely be able to determine if their county or any county contiguous to theirs experienced a D2, D3, or D4 drought. But, it may be unclear in some cases whether a county is within or partly within a drought zone, and for that reason the IRS will publish a list each September of the counties for which a D2, D3, or D4 drought was reported for any weekly period during the preceding 12 months. [\(6\)](#)

### **Q: What is an example of a situation where this election could be applied?**

A: A cow/calf producer residing in a county that has been designated as eligible for federal disaster assistance customarily sells 20 cull cows every year, but due to the drought conditions he or she is forced to sell 60 head this year. The cows sold in excess of the normal number, 40 head, can be considered involuntary conversions. As such, the gain from the sale of those 40 head can be deferred, and will not have to be recognized, as long as the producer uses those proceeds to purchase replacement cows within four years or one year following the first drought free year for his area if a D2, D3 or D4 drought was experienced during the fourth year following the original sale of the animals.

### **Q: What if the value of the replacements is different than the original animals?**

A: In continuing with the example outlined above lets assume that the producer received \$1000/hd for the 40 additional cows he or she was forced to sell in 2011. If this producer was to reinvest more than \$40,000 in 40 cows prior to the conclusion of the drought (as defined above), then the excess would be his tax basis in those cows. However, if that producer reinvests less than \$40,000 in 40 cows at that time, the difference between the amount reinvested and the \$40,000 must be reported as taxable income by amending the 2011 tax return (Form 1040X). [\(5\)](#)

### **Q: What information must be filed for the year in which the animals are replaced?**

A: The following information should be attached to the tax return for the year in which you replace the animals:

- ◆ The date the replacement animals were bought.
- ◆ The cost of the replacement animals.
- ◆ The number and kind of the replacement animals.
- ◆ A copy of the information you attached to the tax return from the year in which you claimed the involuntary conversion. [\(7\)](#)

### **Q: Can I reinvest in something other than livestock?**

A: The replacement livestock must be used for the same purpose as those disposed — i.e., breeding stock must be replaced with breeding stock, and dairy cows with dairy cows. [\(3\)](#) However, a producer may replace livestock with other farm property if, due to drought, flood, or other weather-related conditions it is not feasible to reinvest the proceeds from the sale of the livestock in property similar to or related in use to the livestock. The difficult question is how the IRS will interpret “feasibility”. [\(5\)](#) Consult with your personal tax advisor for more information on this particular issue.

Click on [red underlined](#) links for websites with additional information.

## Visit Hay Hotlines Listed Below for Information on Available Hay

[National Hay Exchange](#) (online resource)

[USDA's Hay Net](#) (online resource)

[Arkansas](#): University of Arkansas Cooperative Extension Service.....(501) 671-2171

[Colorado](#): Colorado Hay Directory .....(303) 239-4115

[Illinois](#) (online resource): Illinois Dept. of Agriculture Hay Directory

[Iowa](#): Iowa Department of Agriculture's Hay Directory .....(515) 281-5321

[Kansas](#): Kansas Farm Bureau in cooperation with Kansas State University.....(785) 587-6000

[Kentucky](#): Kentucky Department of Agriculture.....(800) 248-4628

[Michigan](#) (online resource): Michigan State Extension

[Minnesota](#): University of Minnesota..... (800) 232-9077

[Mississippi](#): Mississippi State Extension.....(662) 325-7718

[Montana](#): Montana Department of Agriculture Hay Hotline.....(406) 444-2402

[Nebraska](#): Nebraska Department of Agriculture.....(800) 422-6692

[Oklahoma](#): Oklahoma Department of Agriculture.....(800) 580-6543

[Tennessee](#) (online resource): Tennessee Farm Bureau

[Texas](#): Texas Department of Agriculture.....(877) 429-1998

[West Virginia](#) (online resource): West Virginia Extension

[Wisconsin](#): Wisconsin Extension Service.....(608) 263-7320

[Wyoming](#): University of Wyoming.....(307) 754-2223

Click on [red underlined](#) links for websites with additional information.

## Tax Option Resources

1. United States Internal Revenue Service. Sales Caused by Weather-Related Conditions. Retrieved on August 6, 2012, from <http://www.irs.gov/businesses/small/industries/article/0,,id=98990.00.html>
2. 26 U.S.C. §451- General rule for taxable year of inclusion. Retrieved August 6, 2012, from <http://www.law.cornell.edu/uscode/text/26/451>
3. 26 U.S.C. §1033- Involuntary conversions. Retrieved August 6, 2012, from <http://www.law.cornell.edu/uscode/text/26/1033>
4. Hobbs, J.C., Tax Consequences of Weather Related Sale of Livestock. Oklahoma Cooperative Extension Service AGEC-788. Retrieved August 6, 2012, from <http://osufacts.okstate.edu/docushare/dsweb/Get/Document-3188/AGEC-788web11.pdf>
5. Green, P. Weather-Related Sales of Livestock. University of Missouri Drought Information. Retrieved August 6, 2012, from <http://extension.missouri.edu/p/AGW1009>.
6. United States Internal Revenue Service. Notice 2011-79: Extension of Replacement Period for Livestock Sold on Account of Drought in Specified Counties. Retrieved on August 6, 2012, from [http://www.irs.gov/irb/2011-41\\_IRB/ar12.html](http://www.irs.gov/irb/2011-41_IRB/ar12.html)
7. United States Internal Revenue Service. Publication 225: Casualties, Disasters, and Thefts. Retrieved August 6, 2012, from <http://www.irs.gov/publications/p225/ch11.html>.