

Example 1. Sale of crops and market livestock.

<u>Description</u>	<u>Quantity</u>	<u>Weight</u>	<u>Price</u>	<u>Total value</u>	<u>Payment terms</u>
Shelled corn	8,700 bushels	-----	\$3.15	\$27,405	when calves sold
Hay	500 bales	70 lb.	2.50	1,250	cash – Feb. 1
Yearlings	50 head	850 lb.	.75	31,875	1/2 on Feb. 1, 1/2 on sale

tion of the weight gain occurring before and after ownership transfer is determined. These percentages determine how much of the added value (sale value minus purchase cost) should go to the younger party and how much to the older party. The amount going to the older party also includes the original purchase cost of the pigs.

This example assumes that the younger party purchases full ownership of the pigs. If the younger party buys only a half interest in the pigs, the same

procedure is used, except only half of the proceeds generated after the ownership transfer go to the younger party (Example 3).

Income tax consequences

The sale of current, non-depreciable assets creates ordinary taxable income for the seller to the extent that the selling price exceeds the basis. For cash basis tax-payers, the basis of purchased property, such as feeder livestock or commercial feed, is the original purchase cost. For raised feed and livestock, the basis is zero. For accrual accounting taxpayers, the basis is the inventory value on the last tax return if the transferred items were owned then, or their purchase cost if they were not.

If the business is organized as a partnership or corporation, the younger party may simply purchase a percent ownership or number of shares in the business. Inventories of crops or livestock would continue to be purchased, owned, and sold by the business entity. The younger party would continue to have a tax basis in a share of the business equal to the purchase price for as long as he/she owns it.

In some cases, assets may be sold below market value to reduce the capital requirements for the younger party. If the assets are significantly undervalued, the IRS may consider that a partial gift has taken place. This may use up some or all of the annual gift tax exclusion (*Information File Gift Tax*) or a portion of the unified estate and gift tax credit (*Information File Federal Estate Tax*).

Summary

When deciding how to transfer machinery and breeding livestock from one party to the next, first consider whether the younger party is committed to

Example 2. Estimating a value for partially finished feeder pigs.

Purchase weight of feeder pigs	50 lb.
Weight at ownership transfer	100 lb.
Sale weight of finished pigs	250 lb.
Purchase cost	\$60 per head
Sale price	\$50 per cwt.
Sale value	\$125 (2.5 cwt. x \$50 per cwt.)
Increase in value (purchase price to sale price)	\$65 (\$125 - \$60)
Total weight gain	200 lb. (250 - 50)
Gain before transfer	50 lb. (100 - 50)
Percent gain before transfer	25% (50 lb. ÷ 200 lb.)
Gain after transfer	150 lb. (250 - 100)
Percent gain after transfer	75% (150 lb. ÷ 200 lb.)
Buyer's proceeds	\$48.75 (\$65 x 75%)
Seller's proceeds	\$76.25 (\$65 x 25%) + \$60
Total proceeds	\$125 (\$48.75 x \$76.25)

Example 3. Partial transfer of feeder pigs (50%).

Buyer's proceeds	\$24.37 (\$65 x 75% x .5)
Seller's proceeds	\$100.63 (\$65 x 25%) + (\$65 x 75% x .5) + \$60
Total proceeds	\$125 (\$24.38 + \$100.63)

farming, and whether his/her financial resources permit an immediate or a gradual transfer. Then, income tax consequences for both the buyer and the seller should be considered for each of the possible transfer methods. Generally, income tax payments can be escaped only by gifting assets, but a gradual sale or lease/buy agreement can postpone tax liabilities for several years.

Regardless of the type of transfer agreement used, a written record of all terms and transactions and an accurate description of the property involved should be maintained for tax and other business purposes.

. . . and justice for all

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