

TIME TO SELL THE FARM?



BY ANDY BIEBL

No one knows when land values will peak, but consider the consequences should capital gain rates change.

Let's begin with the obvious disclaimer: I own no crystal ball that predicts when farmland values will be at their peak. Remember, this is a tax column, so the topic is combining today's high land prices with historically low capital gain rates—rates that may be close to an end.



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ECONOMIC CYCLES. As close as I'll come to any commentary on land values is simply to point to history.

When scarcity drives up the price of goods, the market responds by increasing production, creating substitutes, etc. Land prices are driven by the grain we "manufacture" on that land. The inevitable laws of supply and demand will affect the pricing of that manufactured product, and ultimately the pricing of land.

TAX CYCLES. We have also seen cyclical ups and downs in capital gain rates in this country. About 20 years ago, we had a capital gain rate as high as 28%, but in recent years we have been at a flat 15%.

So what's in store? When the leading Democratic presidential candidates were surveyed during the Iowa campaign, they were both forthright and consistent. If elected president, they said, they would propose capital gain rates between 20 and 28%. Given the present makeup of the House and Senate, unlikely to change in 2009, those increased rates would be enacted retroactively to Jan. 1, 2009. So that leaves 2008 as possibly—or even probably—the last year for a low capital gain rate.

WHO SHOULD SELL? The risk of higher capital gain rates, of course, is only a threat to those contemplating a sale in the immediate years ahead. If you're that retiree considering whether it's time to sell another land parcel to the next generation, or if it's finally time to get off the farm and move to town, you are a candidate.

On the other hand, if the objective is to continue renting the land and pass it down a generation after your estate, stay put. Land passing through an estate receives a step-up in tax basis equal to its estate market value, and a post-death sale is generally done with no capital gain.

THE INSTALLMENT SALE TRAP. Historically, when Congress changes capital gain rates either up or down, gains recognized in the current year are taxed at the current rate. Thus, those collecting on installment sale contracts may walk into future higher rates.

Conventional wisdom suggests taxes are minimized by spreading gains out over several years. But that's fallacy with a flat 15% capital gain rate. Fifteen percent is 15%, whether spread into several tax returns or spiked into one year.

In fact, with various "high-income phaseouts" that erode other deductions in a big income year, a taxpayer is generally ahead to only have a single high-income year rather than multiple years with gains.

So don't get confused about the merits of an installment sale. In a flat capital gain rate environment and more so when rates increase, a single large capital gain—such as 15% in 2008—can be efficient.

As always, run the numbers with your tax pro. With today's software, it is easy to run several "what if" computations and see what works best in your situation. ☺

A leading authority on agricultural tax, Andy Biebl is a principal and CPA with LarsonAllen, one of the nation's top 20 accounting firms. He has co-authored numerous technical guidebooks on ag taxation and is a frequent speaker at seminars and conferences across the country. If you have questions, comments or suggestions for Andy, you can reach him at AskAndy@dtm.com. Individual replies are not possible due to the volume of correspondence. However, he will select the best questions for his bimonthly column that appears on DTN's business page at www.dtnag.com