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Beginning Farmer and Farm Asset Owner Tax Credits (General Fund Taxes -- Income and Franchise Taxes)

[LFB 2009-11 Budget Summary: Page 272, #23]

CURRENT LAW

Under current law, gross business income is income that is generated by a taxpayer in the active conduct of a trade or business. Business income includes gross profit, dividends, interest, rents, royalties, capital gains or losses, and other income.

Under current law, an individual can deduct the costs of qualifying work-related education as a business expense if it meets one of the following two tests: (a) the education is required by an employer or the law to keep the individual's present salary, status, or job; or (b) the education maintains or improves skills needed in the individual's present work. However, even if the education meets one or both of theses tests, it is not qualifying work-related education if it: (a) is needed to meet the minimum educational requirements of the individual's present trade or business; or (b) is part of a program of study that will qualify the individual for a new trade or business.

GOVERNOR

Create a refundable beginning farmer tax credit and a refundable farm asset owner tax credit under the state individual income and corporate income and franchise taxes, including the individual income minimum tax, for tax years beginning after December 31 2010. Because the tax credits would first apply to tax years beginning after December 31, 2010, there would not be a fiscal effect during the 2009-11 biennium. However, the tax credits would reduce individual and corporate income and franchise revenues by an estimated $700,000 in 2011-12, and $1,000,000 annually thereafter.

DISCUSSION POINTS

1. The beginning farmer tax credit would equal the amount paid by the beginning farmer to enroll in a financial management program in the year to which the claim related. The credit could be claimed on one-time basis, and the maximum credit that could be claimed would be $500.

The farm asset owner tax credit would equal 15% of the lease amount received by an established farmer in the year to which the claim related. The credit could only be claimed for the first three years of any lease of the established farmer's assets to a beginning farmer. Both credits would be refundable. If the allowable amount of the credit claim exceeded the income taxes otherwise due, a check would be issued for the difference. The credits would be paid from a newly-created sum-sufficient GPR appropriation.

Partnerships, limited liability companies (LLCs), and tax-option corporations could not claim the farm asset owner tax credit, but the eligibility for, and the amount of the credit would be based on the amounts received by the entities. A partnership, LLC, or tax-option corporation would compute the amount of credit that each of its partners, members, or shareholders could claim and provide that information to each of them. Partners, members of LLCs, and shareholders of tax-option corporations could claim the credit in proportion to their ownership interests.

Tax credits would have to be claimed within four years of the due date for the claimant's tax return. Along with an income tax return, a claimant would be required submit to DOR the certificate of eligibility provided to the claimant by the Department of Agriculture, Trade, and Consumer Protection (DATCP). A part-year resident or a nonresident could not claim the credit. The right to file a tax credit claim would be personal to the claimant, and would not survive the claimant's death. However, if a claimant died after having filed a timely credit claim, the credit would be disbursed to the claimant's personal representative, or surviving relative as provided under current law. The right to file a claim could be exercised on behalf of a living claimant by the claimant's legal guardian or attorney-in-fact.

Current law provisions related to change of ownership and timely filing of claims would apply to the beginning farmer and farm asset owner tax credits. DOR would have full power to take administrative action, conduct any procedure, and to proceed as authorized under the state income and franchise tax laws.

In order to claim a tax credit, both a beginning farmer and an established farmer would have to apply to be certified by DATCP, after review of the application. A beginning farmer would be required to include all of the following in an application:

a. The beginning farmer's name and address.

b. Information showing that the beginning farmer met the definition of a "beginning farmer".

c. A business plan that included a current balance sheet and projected balance sheets for three years, cash flow statements, and income statements along with a detailed description of all significant accounting assumptions used in developing the financial projections.

d. A description of the beginning farmer's education, training, and experience in the type of farming in which the beginning farmer used the leased agricultural assets.

e. A copy of the beginning farmer's completed federal profit or loss from farming form, schedule F, or other documentation approved by DATCP.

f. Any other information required by the DATCP.

To claim the beginning farmer educational credit, the beginning farmer would be required to include in the application, a description of the financial management program completed and a statement of the amount that the beginning farmer paid the educational institution to enroll in the financial management program. DATCP would provide a beginning farmer with a certificate of eligibility for the educational credit, if the Department had issued a certificate of eligibility for the experienced farmer from whom the beginning farmer leased farm assets, and the information provided regarding the financial management program showed that the beginning farmer had completed the program.

An individual would be a beginning farmer if, at the time the individual submitted an application, all of the following applied: (a) the individual had a net worth of less than $200,000; (b) the individual had farmed for fewer than 10 years out of the preceding 15 years; (c) the individual had entered into a lease for a term of at least three years with an established farmer for the use of the established farmer's agricultural assets; and (d) the individual used the leased agricultural assets for farming.

An established farmer would be required to include in the application for certification the established farmer's name and address, information showing that the established farmer met the definition of established farmer, a description of the leased agricultural assets and their location, a copy of the lease, and any other information required by DATCP. The Department would provide an established farmer with a certificate of eligibility for the farm asset owner tax credit if all of the following applied: (a) the established farmer's application included the required information; (b) the beginning farmer's application included the required information; and (c) DATCP determined that the business plan submitted and the education, training, or experience described in the beginning farmer's application showed that the beginning farmer has sufficient resources and education, training, or experience for the type of farming in which the beginning farmer used the leased agricultural assets.

A person would be an established farmer if, at the time the person submitted an application, all of the following applied: (a) the person has engaged in farming for a total of at least 10 years; (b) the person owned agricultural assets; and (c) the person had entered into a lease for a term of at least three years with a beginning farmer for the use of the person's agricultural assets by the beginning farmer.

DATCP would be authorized to approve providers of courses in farm financial management for the purposes of the beginning farmer educational tax credit. The Department could also assist beginning farmers in developing business plans and in the negotiation of leases of farm assets that could enable persons to qualify for tax credits.

"Agricultural asset" would mean machinery, equipment, facilities, or livestock that was used in farming. An "educational institution" would include the Wisconsin Technical College System, the University of Wisconsin-Extension, the University of Wisconsin-Madison, or any other institution that would be approved by DATCP. The definition of "farming" would be referenced to the Internal Revenue Code and would mean the cultivation of land or the raising or harvesting of any agricultural or horticultural commodity including the raising, shearing, feeding, caring for, training, and management of animals. "Financial management program" would mean a course in farm financial management that was offered by an educational institution.

2. Basically, the beginning farmer tax credit program would include: (a) a three-year tax credit for established farmers who enter into a long-term lease with a beginning farmer; and (b) a one-time tax credit for beginning farmers to help offset the cost of a farm management course. To be certified as eligible for the tax credit by DATCP, a beginning farmer would have to include with the application for certification a written multi-year lease agreement between the owner of the agricultural assets and the beginning farmer.

3. According to DATCP, the goals of the proposal include:

a. To provide incentives for beginning farmers to invest in educational programs that will increase the likelihood of their success, and the profitability of their farming activities.

b. To improve the financial position of beginning farmers.

c. To provide an additional source of assistance for individuals interested in entering farming

4. An estimated 800 individuals start in farming annually in Wisconsin. DATCP projects that 400 to 500 of those individuals would be eligible to claim beginning farmer tax credits. However, the Department estimates that 300 individuals would apply for tax credits in the first year and 200 in following years.

5. Nebraska created a beginning farmer tax credit program in 1999. Iowa has a similar program. Both programs generally require the asset owners and beginning farmers to submit applications that include a statement of financial condition (balance sheet). Both states require the beginning farmer to provide certification that they have sufficient education, training and/or experience in the type of farming for which the tax credit will be provided. Both states also allow leases between closely related parties, and land leases. The proposed Wisconsin program would not allow land leases. If allowed, such leases could significantly increase the cost of the program.

Nebraska also requires the beginning farmer to provide a cash flow analysis, and copies of the farm's nutrient management and soil conservation plans. Iowa requires the beginning farmer to provide a copy of Schedule F each year, and charges a $200 application fee for administrative costs. Nebraska does not charge an application fee.

According to the most recent annual program report for the Nebraska program, 58 beginning farmers were approved for the credit during the six years between 2001 and 2006. In the five tax years from 2001 to 2005, asset owners received credits totaling $257,300, or and average of $51,500 per year. Because these participation rates fell short of expectations, the Nebraska program was revised to try to increase participation.

6. The U.S. Department of Agriculture, Farm Service Agency (FSA) provides a number of loan and loan guarantee programs that could provide assistance to beginning farmers including:

a. *Land Contract Guarantee Program.* The program provides "prompt payment" or a 90% principal loan value guarantee to landowners willing to sell land to beginning farmers or ranchers on land a contract.

b. *Direct Operating Loans.* FSA provides loans, of up to $300,000, that can be used to purchase livestock, farm equipment, feed, seed, fuel, insurance, or for other operating expenses. Operating loans can be used to pay for minor improvements to buildings, costs associated with land and water development, and to refinance debts under certain conditions. A five-year line of credit is also available. Graduation to guaranteed or commercial credit is required after seven years.

c. *Guaranteed Operating Loans.* FSA provides a guarantee up to $1,094,000 to local lenders of 95% of loans to farmers. Interest rates cannot exceed the lender's average farm customer rate.

d. *Direct Ownership Loans.* Loans of up to $300,000 can be used to purchase farmland, construct or repair buildings, or promote soil and water conservation. Program eligibility includes sufficient education, training, and managing a farm, and participation in the operation of farm or ranch for three out of the past 10 years.

e. *Ownership Down Payment Loan Program.* FSA requires the beginning farmer to provide a 5% down payment, and then will provide up to 45% toward the purchase of farmland, not to exceed the appraised value and $500,000. As result of the $500,000 cap, the FSA loan maximum is $225,000, but this is not a limit on the value of the land to be acquired. Other financing sources may be used.

f. *Ownership Joint Financing 50/50 (Joint Participation) Loans.* FSA will provide the beginning farmer with up to 50% of financing at an interest rate the same as that provided under the direct farm ownership loan program. No down payment is required.

g. *Ownership Guaranteed Loans.* These loans are similar to guaranteed operating loans.

ALTERNATIVES

1. Approve the Governor's recommendation to create a refundable beginning farmer tax credit and a refundable farm asset owner tax credit under the state individual income and corporate income and franchise taxes, including the individual income minimum tax, for tax years beginning after December 31 2010.

2. Delete the Governor's recommendation.

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