CR-755
0783

OSU Current Report

Cooperative Extension Service • Division of Agriculture • Oklahoma State University

TAX IMPLICATIONS OF RECEIVING PIK GRAIN

Mike L. Hardin, Kim Anderson
OSU Extension Economists

The Payment-In-Kind (PIK) program has created many management decision alternatives for Oklahoma producers. Participation in the PIK program may create different alternatives for each producer. The method of receipt of PIK grain will depend on past participation in the farmer owned reserve or the (Commodity Credit Corporation) loan program, and the availability of grain in a particular area. Taxation of PIK grain will also depend on past participation in the farmer-owned reserve and Commodity Credit Corporation (CCC) loan program, and the election to treat loan proceeds as income in the year of loan receipt or in the year of loan redemption.

It is critical that producers understand the procedure for taking possession of PIK wheat. Taking delivery too soon could cost the producer several cents per bushel. Producers will receive PIK wheat in one of three forms, either a warehouse receipt, a letter of entitlement or by placing their 1983 crop in the regular loan and receiving that wheat for PIK payment.

Warehouse Receipt

Producers who have outstanding loans or farmer-owned-reserve wheat eligible for PIK will be notified that the warehouse receipt(s) are to be picked up at the county ASCS office. The producer accepts title to the grain and is responsible for storage and handling from that time on. Thus, CCC storage payments stop when the producer takes possession of the warehouse receipt(s).

Also, the producer must pay ASCS for all unearned storage on the PIK wheat. For example, if storage has been paid a year in advance and nine month storage remains, the producer must reimburse ASCS for the nine months storage.

Letter of Entitlement

Some producers without eligible loan or farmer-owned-reserve grain will be issued a letter of entitlement. The letter will tell the producer how much grain he is receiving, the grade or quality, how many bushels and where the grain is located. The letter must be taken to the warehouse to claim entitlement. When entitlement is claimed the producer will be given a warehouse receipt for the grain and all CCC storage payments will stop. Thus, when the producer receives the warehouse receipt, responsibility for storage and other costs begins.

New Crop Wheat

If loan or reserve wheat is not available, the CCC can require a producer to place sufficient quantities of the 1983 crop into the regular loan program to meet PIK needs. The producer would be issued a warehouse receipt that could be picked up when possession was desired. Thus, five months free storage could be obtained by not accepting the warehouse receipt until December 1, 1983.

Important Point

Producers receiving warehouse receipts should not pick up the receipt from the local ASCS office or producer with letters of entitlement should not claim entitlement to the wheat until they plan to sell or December 1, 1983, whichever comes first.

PIK PROGRAM TAXATION

The payment-in-kind Tax Treatment Act of 1983 (Public Law 98-4) was signed on March 11, 1983. This legislation provides that payment-in-kind (PIK) benefits received will not be taxed until the commodity is sold. PIK commodities are treated as if they had been produced on the farm. When PIK commodities are sold, they are subject to tax.

Commodity Credit Corporation Loans Affect Tax Treatment

Farmers who received Commodity Credit Corporation (CCC) Loans can elect to treat the loan proceeds as income in the year the loan is received or when the loan is repaid or redeemed. Participation in the PIK program requires that CCC-Loans be redeemed or repaid up to the amount of grain due under the PIK program.

Income in Year Received:

If the CCC-Loan proceeds were included in income in the year received, there is no tax liability when the loan is paid, redeemed, or forfeited. If the grain is sold for more than the amount of the loan, then that amount (sale value less loan value) would be included in taxable income.

Income in Year Repaid or Redeemed:

If loan proceeds received in a previous year were not included in taxable income, the amount must be included in income when the grain is sold and the loan is repaid, redeemed or forfeited. Participation in the PIK program will create a tax liability when the CCC-Loan is forfeited. However, redemption of the loan in this situation will always create a tax liability independent of PIK Program participation

If loan or reserve wheat is not available and CCC requires the producer to place 1983 crops in loan to meet PIK needs, then the simultaneous receipt of the loan proceeds and forgiveness of the loan will create a tax liability equal to the loan amount. The PIK grain will not be included in taxable income until that grain is sold.

Estate Taxes

The new law provides that real property removed from production by participation in the PIK Program will be treated as used in active farming for installment payment of Estate Taxes. Special use evaluation requires that a farmer must have materially participated in farming the property for five of the eight years before his death. The new law makes it clear that if a farmer participates in the PIK Program, the farmer will materially participate in the conservation use that PIK requires on the idle land, thus the Estate Tax Break will not be lost.

In a recent ruling (announcement 83-43, IRB 1983-100) IRS says that farmers will not lose Estate Tax Breaks because of participation in any Government Acreage Diversion Program. This is the case even if an entire farm is removed from production under a Government Diversion Program. And if a farmer's heirs participate in any land diversion program they are also considered to be using the land for a farm use. Thus, there will be no increase or acceleration of Estate Tax as a result of heirs participating in PIK or any other similar program.

Gross Income From Farming:

The new law provides that for all tax purposes, commodities received from the program are treated as if produced by the farmer. Thus, income from 1983 PIK-Commodities will be treated as gross income from farming in the year it is subject to Income Tax. This general provision has wide ranging effects, depending on any previously established tax reporting options utilized by the taxpayer.

Self Employment Tax:

Income from commodities received under the PIK Program will be treated as earned income for those who materially participate in the conservation use of the diverted acreage. As a result, this income is subject to self-employment or Social Security Tax.

Soil and Water Conservation Expenditures:

Farmers can elect to deduct the cost of certain conservation improvements made to farm land. The deduction is limited to 25% of Gross Income from farming. The new law insures that PIK income will be included in the Gross Income used to compute the deduction for land clearing expenditures.

Estimated Tax:

Generally, farmers do not have to pay quarterly estimated taxes. However, to be exempt, 2/3 of a farmer's gross income must be from farming. The new tax law makes it clear that income from PIK commodities counts toward meeting the 2/3 test.

ANTI-SPECULATION RULES

The new law contains an Anti-Speculation rule designed to limit PIK tax benefits to farmers alone. The tax break applies to farmers who own their property on or before February 23, 1983. Exceptions include: (1) Transfers of land by death, gift, or sale to a family member after February 23, 1983. The producer will be taxed on the value of any PIK commodities as of the date of the right to receive them. The Anti-Speculation Rules will prevent a legitimate farmer who purchases land after this date from postponing the tax liability until the PIK commodities are sold.

For more information contact your local Extension County Director, or Area Farm Management Specialist.

Oklahoma State Cooperative Extension Service does not discriminate because of race, color, or national origin in its programs and activities, and is an equal opportunity employer. Issued in furtherance of Cooperative Extension work, Acts of May 8 and June 30, 1914, in cooperation with the U.S. Department of Agriculture, Charles B. Browning, Director of Cooperative Extension Service, Oklahoma State University, Stillwater, Oklahoma. This publication is printed and issued by Oklahoma State University as authorized by the Dean of the Division of Agriculture and has been prepared and distributed at a cost of $295.00 for 5,700 copies. 0883 CC