



# Cattle Producer's Handbook

Drought and Other Natural Disasters Section

980

## Weather Related Sale of Livestock and the Tax Implications

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Occasionally, due to weather related events (drought, flooding, other), stockmen may be forced to sell more offspring or breeding stock than planned. The Internal Revenue Service (IRS) allows this to be treated as an involuntary conversion if four rules are met. The rules only apply to animals sold in addition to the normal course of business. The income from these animals may be deferred to the next year if:

1. Your principal business is farming/ranching.
2. You use the cash method of accounting.
3. You can show that under normal circumstances the sale would not have occurred this year except for the weather-related conditions.
4. The weather-related condition has resulted in your area being designated as eligible for assistance by the federal government.

Sales made before the area became eligible for federal assistance still qualify as long as the weather event that caused the sale also caused the area to be designated as eligible for federal assistance. The designation can be made by the President, the USDA or any of its agencies, or other federal agencies.

### Usual Business Practice

You will need to determine the number of animals you would have sold under normal conditions following usual business practices. Only the income or gain from selling animals **over and above** what would have occurred in a normal year is allowed.

If you are faced with weather-related sales in more than one year, a separate election must be made for each year. If you make this choice in successive years, there are special rules that prevent your choice in the first year from adversely affecting your choice in the second year.

- Do not include the amount deferred from one year to the next with the sale or exchange of livestock in the later year when figuring the amount to be postponed.
- In determining your normal business practice for the later year, exclude any earlier year for which you make this choice.

In order to make the election to postpone reporting income from weather-related sales of livestock, you must attach a statement to your tax return for the year of the sale. The statement must include your name, address, and Social Security number and the following information about each class of animals sold:

1. A statement that you are making an election under section 451e.
2. Evidence of conditions that forced the early sale and the date, if known, that the area was designated eligible for federal disaster relief.
3. An explanation of the area affected by weather-related conditions leading to your early livestock sale.
4. The number of livestock sold in the three preceding years.
5. The number you would have sold in this tax year had you followed normal business practices.
6. The total number sold and the number sold because of weather-related conditions.
7. A computation of the income to be postponed for each class of livestock.

The statement and return must be filed by the due date of the return, including extensions. If you filed your return on time for the year without making the choice, you can file an amended return within 6 months of the due date (excluding extensions). Attach the statement to the return and write "Filed pursuant to section 301.9100-2" at the top of the statement.

## Connection with Affected Area

The livestock do not have to be raised or sold in a weather-related area to qualify for the postponement. The livestock producer qualifies for postponement if the sale occurred solely because of weather-related conditions that affected the water, grazing, or other requirements of the livestock so that the sale became necessary.

The election and the amount calculated to be postponed must be made separately for each generic class of animals such as hogs, sheep, or cattle. The amount to be postponed for each class can be calculated as follows:

- Divide the total income realized from the sale of all livestock in the class during the tax year by the total number sold, and
- Multiply the result by the excess number of animals sold because of the weather-related conditions.

### Example

As a calendar year taxpayer, you normally sell 105 head of calves and 15 cull cows during the year. Because of a drought, you sell 135 calves and 25 cows during the year. You receive \$63,110 from the sale of calves and \$10,500 from the sale of cows. Because the government declares the area eligible for drought assistance, the income you may elect to postpone until next year is:

Calves: \$14,024  $(63,110 \div 135 \times 30)$

Cows: \$4,200  $(10,500 \div 25 \times 10)$

A total of \$18,224 may be postponed one year.

## Replacement Stock and Reporting a Gain from Involuntary Conversion

If solely because of weather related conditions (e.g., drought or flood) you sell or exchange livestock held for draft, breeding, or dairy purposes you may treat the sale as an involuntary conversion. Only livestock sold in excess of the number you normally would sell under

normal business practices are considered involuntary conversions. The rules for ordinary gain or loss (Ch. 10, Farmers Tax Guide) apply unless the livestock is later replaced. Gains and losses from breeding livestock sales are reported on Form 4797.

You postpone gain by reporting your choice on your tax return for the year in which you receive the gain (insurance proceeds, sale of stock, other). The statement should include:

- The date and details of the involuntary conversion,
- The reimbursement received,
- How you figured the gain.

Taxpayers have up to 2 years from the time of forced sale to replace stock sold due to a weather-related condition. The replacement period begins on the date the livestock were sold, exchanged, or damaged or destroyed. The period ends 2 years after the close of the first tax year in which you realize any part of the gain from involuntary conversion.

Replacement property must be purchased with the specific purpose of replacing your property. The replacement property must be similar or related in service or use to the property it replaces. Property acquired as a gift or inheritance does not qualify as replacement property.

Special rules may also apply if buying replacement property from a relative. In the year replacements are purchased for livestock sold due to weather-related conditions the tax return should have a statement with information on:

1. The date replacement livestock was purchased.
2. The cost of replacement livestock.
3. The number and kind of replacement livestock.

If the purchase cost of replacements is less than the receipts from the sale of the livestock due to weather-related conditions the excess is a taxable gain and must be reported as income.

A general explanation of weather-related sale procedures is in the Farmers Tax Guide (IRS Pub. 225) in chapters 4 and 13. It is always advisable to consult with a reliable accountant and federal agency representatives.

