


FSA Payment Limitation Rules
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2008 Farm Bill

- Included changes to Payment Limitation Rules
 - Large producers hardest hit
 - Rules are simpler and more straight forward (but still complex)
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Review of Eligibility

- **Varies by Program**
 - **For Direct, Counter Cyclical, and ACRE Payments**
 - 1. Must not exceed income levels**
 - 2. Must be actively engaged in farming**
 - **Contribute Labor and/or Management and**
 - **Capital, Land, and/or machinery**
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Income Rules

If average adjusted gross...	Person/Entity is ineligible for...
NON-FARM income exceeds \$500,000	Commodity, price support and disaster assistance. Direct, Counter-Cyclical, ACRE, LDP, etc...
FARM income exceeds \$750,000	Direct Payments
NON-FARM income exceeds \$1 million	Conservation Programs – EQIP, CRP, etc... (unless 2/3 of AGI is from farming)





Adjusted Gross Farm & Non-Farm Income

- Net Income (Not Gross)
- Three year rolling average
 - For 2009 program, tax years 2005-2007
- Reported to FSA on CCC-926





Adjusted Gross Farm & Non-Farm Income

Adjusted Gross Income

(line 37 on 1040)

- **Adjusted Gross Farm Income**

(line 18) + (lines 13, 14, 17 if farm related)


(deduct "above the line deductions")

= **Adjusted Gross Non-Farm Income**





Adjusted Gross Farm & Non-Farm Income

- Each individual and business entity is subject to income limitations
 - Joint ventures and partnerships not subject to income limitations, only owners
 - Spouses report income together but may split out with certification from CPA or attorney
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Adjusted Gross Farm & Non-Farm Income


- Income Limitations may change for next year







Direct Payments

- Payments made to grain producers regardless of yield, price, or revenue
 - Direct payments are typically \$20 - \$23/ acre in Ohio
 - Direct payments are limited to \$40,000 per person (Payment Limitation)
 - Each person can farm roughly 2,000 acres before payment limitations take effect
 - Other programs have payment limitations but direct payments are the most restrictive
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Direct Attribution Replaces Three Entity Rule

- Previously, a producer could receive a second payment limitation (\$40,000) through the use of up to two additional business entities
 - New rules only allow each tax ID number to receive \$40,000
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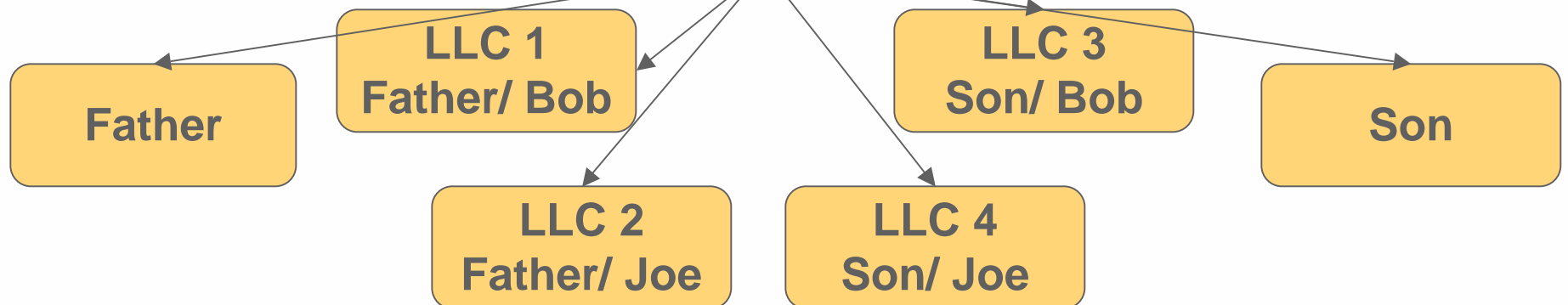
Direct Attribution Replaces Three Entity Rule

- Each entity may receive up to \$40,000
 - **LLC, Corporation, Limited Partnership**
 - Each person may receive up to \$40,000
 - **Regardless of how many entities or farming operations**
 - Partnerships and JV may receive unlimited payments but personal limitations still apply
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The Old Way

\$240,000 in Direct Payments
12,000 acres x \$20/acre

PARTNERSHIP
(Farms 12,000 acres)

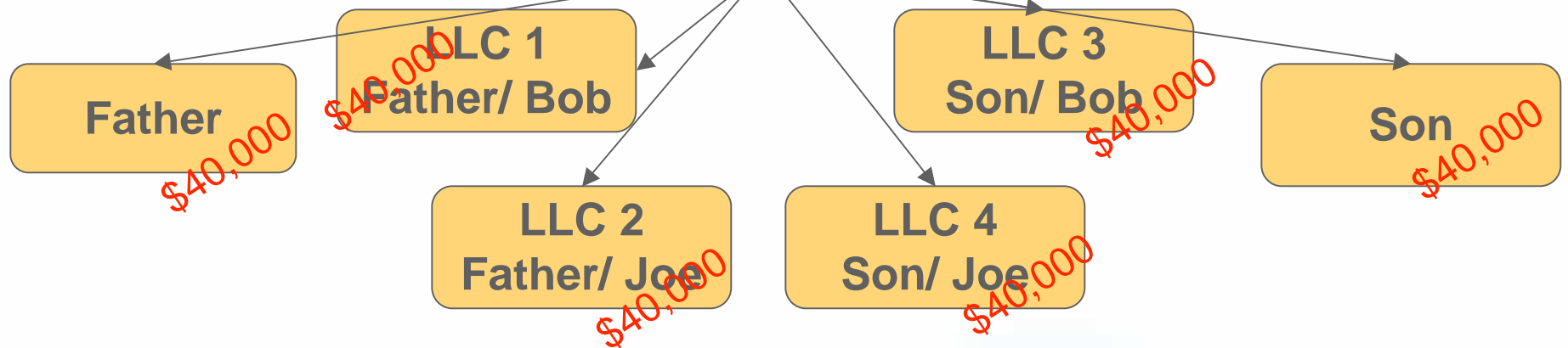


All \$240,000 in Direct Payments Captured by Partnership through the use of multiple entities

The Old Way

\$240,000 in Direct Payments
12,000 acres x \$20/acre

\$240,000
PARTNERSHIP
(Farms 12,000 acres)



All \$240,000 in Direct Payments Captured by Partnership through the use of multiple entities



The New Way

\$240,000 in Direct Payments
12,000 acres x \$20/acre

PARTNERSHIP
(Farms 12,000 acres)

Father

Mother

Son

Daughter-in-law

Each person receives \$40,000

leaving \$80,000 unusable



The New Way

\$240,000 in Direct Payments
12,000 acres x \$20/acre

\$160,000 PARTNERSHIP
(Farms 12,000 acres)

Father

\$40,000

Mother

\$40,000

Son

\$40,000

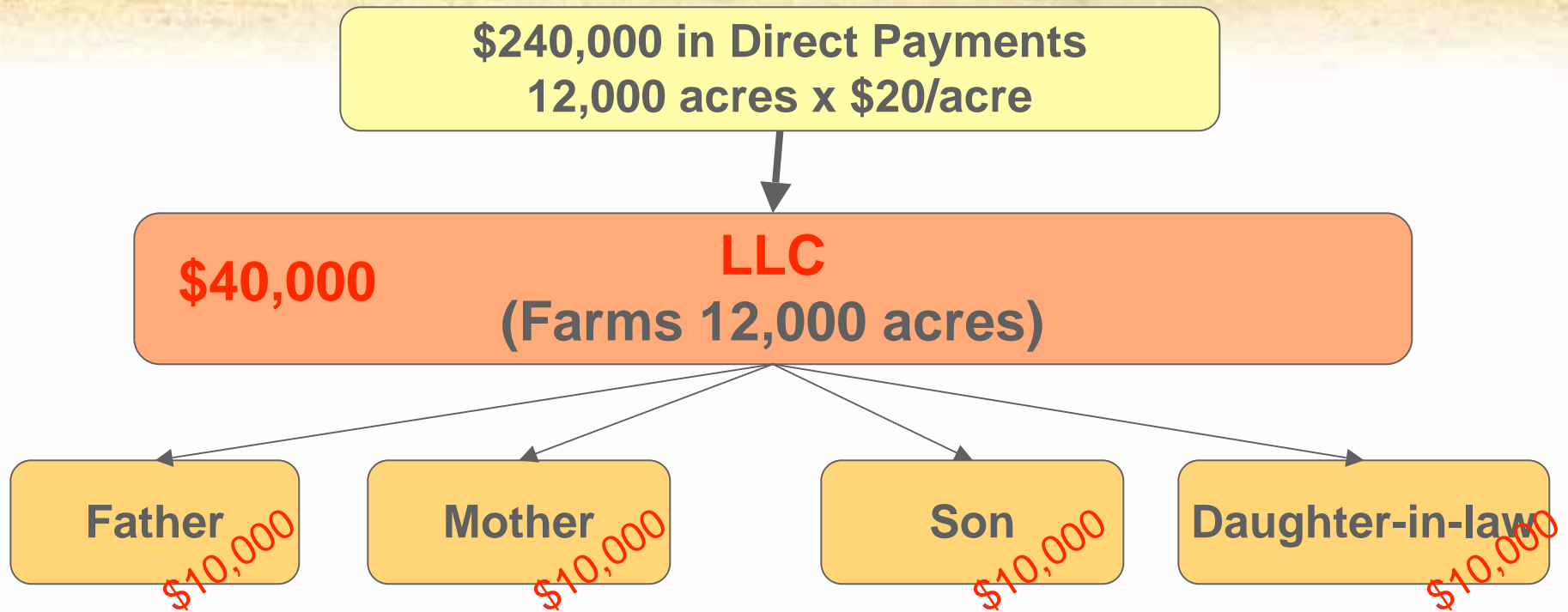
Daughter-in-law

\$40,000

Each person receives \$40,000

leaving \$80,000 unusable

The Problem with Entities



The LLC is eligible for \$40,000 leaving \$200,000 unusable

Capturing Direct Payments leads to otherwise poor business planning!



Requirements for “Actively Engaged in Farming”

- Right Hand Side Contribution
 - Labor and/or Management
- Left Hand Side Contribution
 - Land, Capital, and/or Machinery






Requirements for “Actively Engaged in Farming”

- **Exceptions**
 - **Landowner**
 - Contributes land and is paid based on performance of farming operation
 - **Spouse**
 - A spouse of a producer actively engaged in farming is credited with producer’s labor and management for same farm operation
 - Must still contribute land, capital, and/or machinery
 - **Adult child**
 - Only required to contribute labor/ management






New Rules for Spouses

- Spouses now qualify for direct payments more easily
 - If a producer is actively engaged in farming, the spouse automatically is credited with the producer's labor and/or management
 - Spouse must still contribute his/her share of capital, land, and/or machinery
 - Not helpful to single producers and producers not interested in have spouse in ownership
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Business Entities

- **Actively Engaged in Farming**
 - **Regulations and Handbook states all members with an ownership interest must contribute labor and/or management to be “actively engaged in farming”**
 - **Regulations and Handbook also state that an entity’s payment will be reduced by the pro rata share of an owner not contributing labor and/or management**
 - **Do entities with an inactive owner qualify for direct payments?**
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Dealing with Lack of Payment Limitations

- Add partners to a partnership
 - each partner must be actively engaged in farm
 - Can be challenging for new member to become equal owner (child buying into \$\$\$ operation)
 - If not family member, requires substantive change (add 20% land, change in ownership, addition of equipment)
 - Set up new farming operation or entity
 - Difficult to do if new operation or entity farms any land previously farmed by old entity
 - New operation must stand on its own, capital becomes a problem
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Dealing with Lack of Payment Limitations


- Convert cash rent landlords to share rent landlords
 - Direct payment is shared with landlord
 - Landlord must sign up for program
 - Could be subject to SE tax and have implications for Social Security

It is not easy to add payment limitations!






Common Mistakes

- Custom Farming
 - Do not hire labor/management and machinery together
 - FSA may consider custom farming and not actively engaged in farming
 - Tainted Financing
 - Farming operation must stand on its own for financing
 - Loan made to, guaranteed by, or secured by a related party may not be a contribution
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Common Mistakes

- **Guaranteed Payments**
 - **Guaranteed payments to a partner eliminates that entire type of contribution**
 - **Draws are no problem**
 - **Leases with related parties in writing**
 - **Must be at fair rate with customary payment terms**
 - **Terms should include price, what is being leased, and time of payment**
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Common Mistakes

- Partnerships with unequal ownership
 - Does not maximize direct payments
 - Number of payment limitations is dependent upon partners' ownership percentage
 - **Example**
 - Partnership has 3 owners, 40-40-20
 - Partnership is only eligible for 2 ½ payment limitations
 - Take ownership % of largest partner and divide into 100
 - $100 \div 40\% = 2 \frac{1}{2}$



Questions?

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Presentation will be available on web site

