

Ag Law and Tax Ramblings

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Overview

This weekend was the annual spring tree planting at the Kansas place. This year a couple of dozen eastern white pines were planted. Normally, the spring planting is a lot more than that, but that's all that was needed this spring. While planting I have time to think about issues that farmers and ranchers face. Now that I am at my desk and looking out at a tom turkey, a crane and two Canadian geese, I can write some of those thoughts out.

Current events and other thoughts in ag law and tax – it's the topic of today's post.

Tariffs and Agriculture

Tariffs have been in the news lately and many questions are being raised about their potential impact on agriculture. Will tariffs be good or bad for agriculture? Look at the issue in the short term and the long term. Largely attributable to poorly structured trade deals over the past 40 years, the U.S. is running a trade deficit with practically every country that it exports ag products to. A major contributor to the problem is the higher tariffs that those countries impose on U.S. ag products coming in compared to the tariffs the U.S. imposes on their ag products exported into the U.S. So, in the long term if the U.S. can achieve parity on tariff rates, that would be good for the U.S. farmer and rancher. Of course, there would be a short-term hit until the tariff rate negotiating is completed.

An interesting economic fact is that the U.S. is not the largest producer of export foods by volume, but it is in terms of value. Half of what the U.S. produces is sold abroad and it's very pricey because many specialty crops are involved. It's not just corn or soybeans or sorghum.

The other thing to keep in mind is tax policy. Tax policy along with downsizing government fits hand in glove with tariff policy. Tariffs can be even more powerful than now if the size of government is decreased. On the tax policy side of the equation, if bonus depreciation is reinstated at 100 percent, the corporate tax rate for domestic production is reduced to 15 percent and non-C corporations get to keep the 20 percent business deduction, the long run could turn out to be pretty good for ag producers. So, all three must work together – tariff parity (leading to reduced tariffs globally), reducing the size of government, and continuing (or making permanent) the Tax Cuts and Jobs Act (and passing the other proposed tax cuts). If all of this can be accomplished, the future looks bright.

Note: USMCA-compliant imports (imports from Canada and Mexico) to the United States on or after March 7, 2025, are exempt from National Emergency Tariffs. Also, President Trump via Executive Order reduced the existing tariffs on potash from 25 percent to 10 percent. *Executive Order of March 6, 2025.*



Deferred Payment Contracts

Many farmers sell grain and livestock and defer payment until the next tax year. Spring is the time many deferred payment contracts are entered into. But, to properly defer the income for tax purposes, certain rules must be followed. So, it's good to review the rules again.

To defer income, a deferred payment contract must be structured properly to prevent IRS from claiming that you must pay tax on the income for the current year even though you didn't actually receive it in the year of sale. There are three key points – don't have the sale income credited to your account; make sure the buyer doesn't set it apart for you, and make sure the buyer doesn't allow you access to the money in the current year if you wanted it.

A properly drafted deferred payment contract can satisfy these requirements. Make sure that the price of the goods is set at the specified time for delivery, but payment is deferred until the next year. The contract must be bona fide and entered into at arm's length, and you must not have any right to demand payment until the following year. That means you can't require payment upon demand. The contract (as well as the sale proceeds) must also be non-assignable, nontransferable and nonnegotiable.

If it turns out you don't want or need to defer, just report the income in the year of sale. If you have multiple crops, use a different contract for each crop. Also remember that you are unsecured until you get paid.

Easement Tax Issues

Rural landowners often receive payments from companies for rights-of-way or easements over their property. The rights acquired might include the right to construct a pipeline, construct aerogenerators and associated roads, electric lines and similar access rights. How are these payments to be reported for tax purposes?

Easement payments may trigger income recognition or could be offset partially or completely by the recipient's income tax basis in the land that the easement impacts. Also, an easement transaction might involve the sale of part of the land or a payment for crop damage.

If the payments are basically rents for land use, then report them as ordinary income. But if you grant a limited easement you'll be treated as having sold a portion of the rights in the land impacted by the easement. That means you can apply the proceeds first to reduce the basis in the land affected with only the excess being taxable as capital gain. If the grant of an easement deprives you of practically all the beneficial interest in the land, but you still hold legal title, you'll be treated as having sold the land that the easement covers. That sale would also be capital in nature.

If you get an upfront payment for granting an easement, report it on Schedule E. Any amount paid for actual, current damage to the property caused by construction activities may be able to be offset by basis in the affected property. A payment for damage to growing crops, however, is treated as a sale of the crop reported either on line 2 of Schedule F or line 1 of Form 4835. Any payment for future property damages, however, is generally treated as rent and reported as ordinary income.



Easements for pipelines, roads, surface sites and similar interests that are for a definite term of years are leases. If property is taken for an easement, any condemnation award paid is treated as a sale for tax purposes. But it might be possible to defer the gain realized from a condemnation by reinvesting the proceeds in qualifying property within three years.

Make sure you get good tax advice before you get involved in an easement transaction.

Warrantless Searches (“Open Fields”) Doctrine

An issue that keeps coming up in different parts of the country involves warrantless searches on farms and ranches. It’s a big concern to rural landowners with significant Constitutional implications.

The government can’t conduct unreasonable searches and seizures. If a person has a legitimate expectation of privacy, the government must get a warrant before conducting a search. But in 1924 the Supreme Court said that the Fourth Amendment protections don’t extend to “open fields” – areas beyond those immediately surrounding and associated with the home. *Hester v. United States*, 265 U.S. 57 (1924). See also *Florida v. Jardines*, 569 U.S. 1 (2013). This is a huge issue of importance to agriculture because over 96 percent of all private land in the U.S. lies outside the “curtilage” (the area immediately surrounding the home). Over the past few years, the issue has seemed to come up more frequently in numerous cases in several states. See, e.g., *Rainwaters v. Tennessee Wildlife Resources Agency*, No. W2022-00514-COA-R3-CV, 2024 Tenn. App. LEXIS 208 (Tenn. Ct. App. May 9, 2024). Those cases point out that state law on the issue matters significantly. Also, some state legislatures have amended existing laws in an attempt to provide greater protection to landowners. Those laws are often directed at state wildlife officials.

If the government seeks entry into such an area, a reasonable reading of the Constitution requires the government to gather probable cause and secure a search warrant before entering. To date, courts in seven states have rejected the open fields doctrine under their own constitutions: Mississippi, Montana, New York, Oregon, Tennessee, Vermont, and Washington. In addition, when a landowner posts property as “No Trespassing,” that posting should be respected, even by the government.

The warrantless search issue will likely continue in the future in the courts and state legislatures. It’s an important issue for farmers, ranchers and rural landowners.

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