

# Department of Agricultural and Resource Economics

---

## LIVESTOCK SALES – UNDERSTANDING TAX IMPACTS

August 2019

*Alan Galloway, Area Farm Management Specialist*

**H**ow farm livestock sales records are kept and the reporting of sales of livestock on an income tax return can have a major impact on taxes owed. Correctly reporting sales that qualify for capital gains treatment can reduce both income and self-employment taxes. This publication reviews the different types of livestock sales and tax impact of the sales. Additional information can be found in IRS publication 225-Farmer's Tax Guide.

### Types of Livestock Sales

Generally there are two types of livestock sales: sales from livestock which are primarily held for that purpose and livestock held for breeding, draft and milking purposes.

### Sales of Livestock

An animal raised or purchased with the objective to sell the animal (market livestock) means the animal is not intended to become breeding livestock (breeding livestock covered later). The income from the sale of market livestock is ordinary income reported on Schedule F (Profit or Loss from Farming). Ordinary income tax rates will apply and the income is subject to self-employment tax.

Income from the sales of livestock held for breeding, draft or milking purposes is not reported on Schedule F and is not subject to self-employment tax. Income from these sales is reported on Form 4797 (Sales of Business Property) and any remaining cost basis is deducted to calculate the gain or loss. Gains and losses from the sales of livestock held for breeding, draft or milking purposes may be short-term or long-term, depending on how long the animal was held and the amount of any depreciation that was previously allowable. Long-term capital gains are generally taxed at lower rates than ordinary income.

Keeping records sufficient to accurately track and communicate sales of these types of animals to one's income tax preparer may reduce taxes owed.

### Livestock Raised for Sale

Income from cattle, sheep, swine or other market animals that are intended to be sold after raising or purchase is generally considered ordinary income. Raised animals have zero cost or basis, as the expense of raising was deducted while the animals were being raised. The cost of any selling expenses are subtracted from the selling price of the raised animal to determine the net income from the sale.

**Example 1.** Farmer A raised a group of calves to 500 pounds each. When sold, the income is reported on Schedule F, line 2 (Sales of Livestock, Produce, Grains and Other Products You Raised). The marketing expenses and transportation costs of selling the animals are deducted as farm expenses on Schedule F.

## Livestock Purchased for Resale

The net income from purchased animals is determined by subtracting the cost of the animal and the selling expenses from the sales price. Sales of market animals are considered ordinary income.

**Example 2.** Farmer B purchased a group of calves at 250 pounds each and sold them when they reached 500 pounds. The income from the sale is reported on Schedule F, line 1a (Sales of Livestock and Other Resale Items). The cost of the calves when purchased is reported on Schedule F, line 1b (Cost or Other Basis of Livestock or Other Items). The difference is reported on Schedule F, line 1c. Other expenses incurred in the feeding, care, marketing and transportation are deducted as farm expenses on Schedule F.

## Breeding, Draft and Milking Livestock Sales

The term “breeding livestock” will be used to describe sales of all livestock held for breeding, draft and milking. The reporting and tax treatment of income from breeding livestock depends on the following factors:

1. Whether the animal was raised or purchased;
2. How long the animal was held for breeding purposes (see holding period below); and
3. Whether the sale resulted in a gain or loss.

Cattle sales are used as examples in this discussion; however, the rules are similar for other types of livestock.

## Raised Breeding Livestock

A farmer has no cost (basis) in a raised animal since the expenses of raising the animal were deducted while it was being raised. The sale of the breeding livestock may result in a taxable capital gain. The sale of the breeding livestock is reported on Form 4797. These sales include cows and heifers raised for breeding purposes, bulls and other cull breeding animal sales.

**Example 3.** Farmer C sold a 4-year-old raised cow for \$1,100. The expenses of the sale are \$125, and these are deducted from the gross sales price to arrive at a gain of \$975. This gain is a long-term gain since the cow was held at least two years and is not subject to self-employment tax. This gain would be combined with other gains and losses to determine net gains and losses for the year. Net long-term gains are taxed at the lower capital gains tax rates (see tax rate tables below).

## Purchased Breeding Livestock

Depending on the purchase and selling price of purchased breeding livestock and the amount of allowable depreciation, the sale of purchased livestock could result in either a taxable gain or loss. Purchased breeding animals can be depreciated like other assets used in a business. The gain or loss is calculated by subtracting selling price from purchase price and adjusting for any allowable depreciation. Gains on the sale of purchased breeding livestock to the extent of allowable depreciation are considered ordinary gains and taxed as ordinary income.

**Example 4.** Farmer D sold a cow purchased four years ago. The cow was purchased for \$1,300 and sold for \$1,250. The amount of depreciation taken was \$867, and the expense of the sale was \$125. The gain from the sale of the purchased cow is calculated as follows:

Gross selling price	\$1,250
Original cost	\$1,300
Add expense of sale	+ 125
Less allowable depreciation	- <u>867</u>
Adjusted basis	<u>\$ 558</u>
Gain realized	\$ 692

The expense of the sale (\$125) is added to the original cost (\$1,300), and the amount of depreciation taken on the cow (\$867) is subtracted to arrive at the adjusted basis of the cow (\$558). The adjusted basis is subtracted from the gross selling price to determine the gain of \$692. This gain is reported on Form 4797.

## Holding Period

The length of time the animal is held on the farm determines whether the sale qualifies as a long-term capital gain. Generally, the holding period is 24 months for cattle and horses and 12 months for other livestock.

Other observations:

- There are some exceptions to the holding period rules for situations like weather-related sales of livestock.
- If an animal (like a heifer) is raised with the intent to sell it for breeding livestock and it is determined the animal is sterile and the animal is sold within a reasonable time, it could be considered breeding livestock.
- A farmer who is selling an entire herd of animals, generally, could consider the younger animals that would have become breeding livestock as such for tax purposes.

## Importance of Proper Reporting

If Farmer D had mistakenly reported the sale of the cow for \$1,250 on Schedule F as raised livestock with no basis, the entire amount would be considered ordinary income and would also be subject to self-employment tax. Depending on the farmer's adjusted taxable income from all sources, if the farmer is in the 10 percent tax bracket, the overpayment of income and self-employment tax in this case could be about \$300.

In years when a farm has an overall loss, improper reporting reduces the loss and could increase taxes owed, as less income from other sources (off-farm, investments, etc.) would be offset by the reduced loss.

## Summary

Farmers should maintain careful records, separating sales of market livestock from sales of breeding livestock. Breeding livestock should be further separated by whether they were raised or purchased. Keeping good records helps farmers minimize their tax burden and helps their tax preparer to have the information needed to complete a correct tax return.

### Tax Rates — Ordinary Income (2019 brackets)

Tax Rate	Single	Married (Joint)
10%	Up to \$9,700	Up to \$19,400
12%	\$9,701 to \$39,475	\$19,401 to \$78,950
22%	\$39,476 to \$84,200	\$78,951 to \$168,400
24%	\$84,201 to \$160,725	\$168,401 to \$321,450

Higher rates apply to higher income levels.

### Long-Term Capital Gains Tax Rates (2019)

Tax Rate	Single	Married (Joint)
0%	Up to \$39,375	Up to \$78,750
15%	\$39,376 to \$434,550	\$78,751 to \$488,850
20%	Over \$434,550	Over \$488,850

Higher rates might apply to collectibles and other specific situations.

## References

Alleman, T. 2012. "Navigating the Tax Maze of Livestock Sales." *Progressive Dairyman*.

Internal Revenue Service Publication 225–Farmer’s Tax Guide. 2018.

Kightlinger, K. 2011. "Income Tax Reporting of Livestock Sales." University of Georgia, Department of Agricultural and Applied Economics, AGECON-11-002.



[AG.TENNESSEE.EDU](http://AG.TENNESSEE.EDU)