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FEDERAL INCOME TAX: SOME CONSERVATION PAYMENTS ARE NOW EXEMPT

General Rule: Before Sept. 30, 1979, the general rule was that government payments for conservation projects were included in the taxpayer's gross income unless specifically excluded. The Revenue Act of 1978 changed the general rule for certain conservation payments for a number of reasons.

Under several programs, state and federal governments share the cost of certain improvements in land by making payments to the participating taxpayer. These programs are of a nature that further conservation, protect or restore the environment, improve forests, or provide habitat for wildlife. These kinds of payments generally do not improve the income-producing capacity of the land.

Congress saw this as a situation where they wanted taxpayers to share in the cost of land improvements for the sake of the general welfare. However, under the general rule, such an arrangement would cause the participating taxpayer to be zapped with higher income taxes, even though his income was not increased. Clearly this would discourage participation. Congress chose to exclude certain conservation cost-sharing payments from income, and to provide that they be included only when the underlying property is sold.

-more-

add one--federal income tax

The New Law: The Revenue Act of 1978 provides that gross income does not include the excludible portion of payments received under the following programs:

1. Rural clean water program of section 208(j) of the Federal Water Pollution Control Act;
2. Rural abandoned mine program of section 406 of the Surface Mining Control and Reclamation Act of 1977;
3. Water bank program of the Water Bank Act;
4. Emergency conservation measures program of title IV of the Agricultural Credit Act of 1978;
5. Agricultural conservation program of the Soil Conservation and Domestic Allotment Act;
6. Great plains conservation program of section 16 of the Soil Conservation and Domestic Policy Act;
7. Resource conservation and development program of the Bankhead-Jones Farm Tenant Act and the Soil Conservation and Domestic Allotment Act;
8. Forestry incentives program of section 4 of the Cooperative Forestry Assistance Act of 1978;
9. Any small watershed program administered by the Secretary of Agriculture which is determined by the Secretary of the Treasury to be substantially similar to the type of programs listed in 1. through 8.; and
10. Any state program under which payments are made primarily for soil conservation, protection or restoration of the environment, improvement of forests or provision of wildlife habitat.

To qualify for exclusion these two conditions must be met:

1. The Secretary of Agriculture must determine that a payment was made primarily for the purpose of conserving soil, protection or restoring environment, improving forests, or providing wildlife habitat; and
2. The Secretary of the Treasury must determine that the payment will not result in a substantial increase in the income-producing capacity of the subject property.

-moreadd two--federal income tax

The U.S. Department of Agriculture has issued proposed criteria for meeting these conditions. Your tax attorney or tax accountant has access to these criteria.

Other Tax Advantages Forgone: When payments are excluded from income under this law, the taxpayer may not claim a current deduction, depreciation, amortization, depletion or investment credit with respect to the subject property. The basis of property purchased or improved with these payments is not affected.

If the subject property is disposed of within 20 years, the income recognized or the excluded payments (whichever is smaller) will be recaptured or treated as ordinary income at the time of the disposition. The amount recaptured will be reduced 10 percent per year after the first 10 years.

This law applies to payments made after September 30, 1979.

Analysis: This new law could result in significant tax savings for some farmers. Some of the lands qualifying for this exclusion will also qualify for the new Minnesota Wetlands Exemption and Credits.

Congress expects this exclusion to reduce federal budget receipts by $28 million in fiscal year 1980 and by $79 million in 1983.

Note: Winston Grant has studied law and holds a masters degree in agricultural economics. He is a six-year staff member of the Department of Agricultural and Applied Economics where he has twice taught an experimental course in agricultural law and coordinates the statewide Law for Laymen program co-sponsored by the Minnesota Bar Association and the Agricultural Extension Service. Readers are invited to send comments and questions to him at that department, University of Minnesota, St. Paul, MN 55108.

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