End-of-Year Tax & Accounting Reminders for Equine Operations

December 5, 2024

Friendly Reminder

The matters discussed today provide general information only. The information is neither tax nor legal advice. You should consult a qualified professional advisor about your situation before taking action.

The focus of today's webinar is equine operations conducted as for-profit businesses.

Objectives

- Form 1099 reporting reminders
- Common Federal tax incentives and considerations:
  - » Depreciation options
  - » BOI reporting reminder
  - » Hobby loss and passive activity rules
- Expiring Federal tax provisions and election impact
- Year-end tax planning items

Form 1099 Reporting Requirements for Equine Industry Participants

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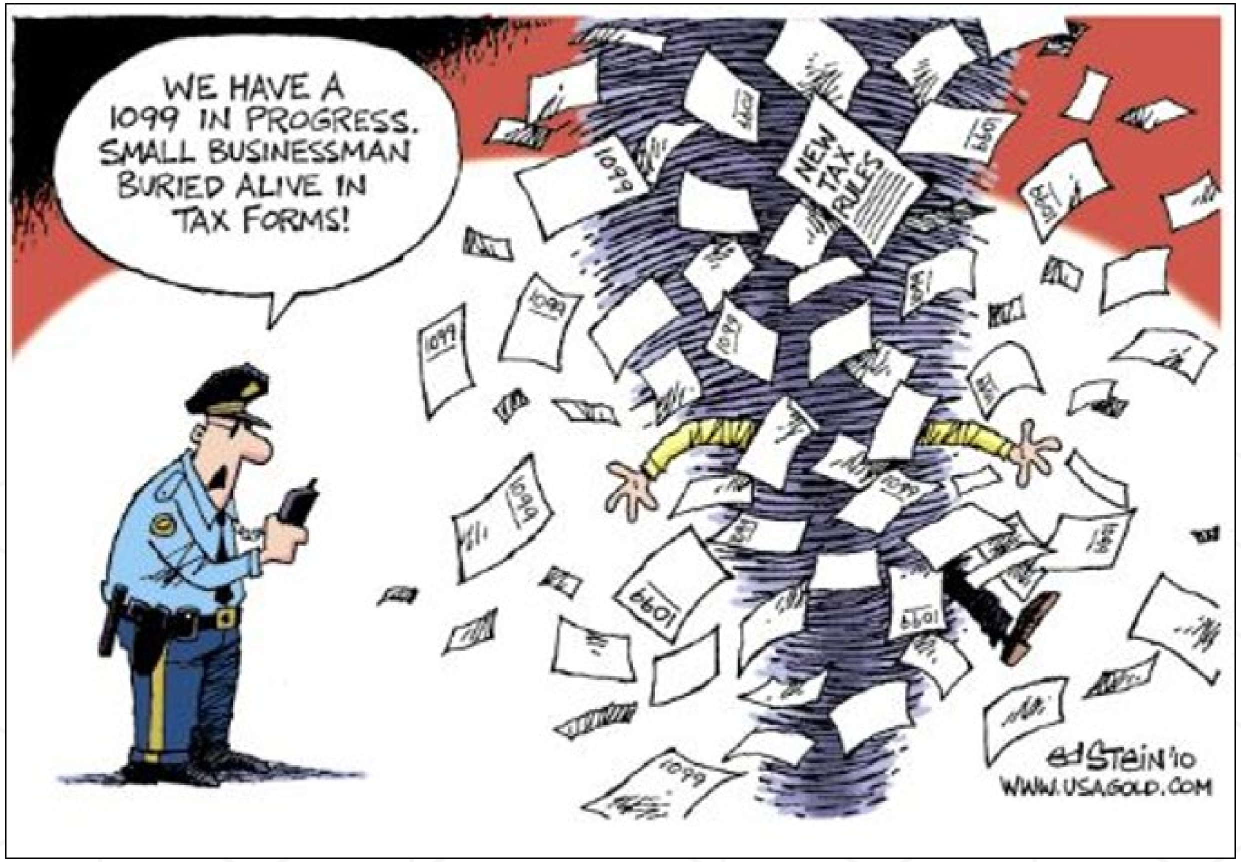
Anyone else in January?



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Objectives

- Why we are here
- Review definitions specific to 1099-MISC and 1099-NEC
- Reporting examples between 1099-MISC and 1099-NEC
- Other reminders

Why do we care about 1099s?

- Required by the IRS
- Makes life easier for your recipient
- Avoid penalties and IRS notices

Definitions

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1099-NEC Definition

If the following four conditions are met, you must generally report a payment as NEC.

- You made the payment to someone who is NOT your employee
- You made the payment for services in the course of your trade/business
- You made the payment to an individual, partnership, estate and in some cases, a C corp
- You made payments to the payee of at least $600 during the year

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1099-MISC Definition

Report on Form 1099-MISC only when payments are made in the course of your trade or business.

Personal payments are not reportable

You made the payment for services in the course of your trade/business

You made the payment to an individual, partnership, estate and in some cases, a C corp

You made payments to the payee of at least $600 during the year

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Reporting Examples

1099-NEC Equine Related Vendors

Types to include in Box 1,

DO NOT SEND if confirm business is INCORPORATED*

Training

Boarding

(usually include all items on monthly statements; items NOT included are stud fee payments or horse purchases)

Vanning

Farrier

Contract Labor

Repair Services

Consulting

Legal/Attorney*

Accounting

Lawn Services

Chiropractic

Podiatry

Equine Spa

Electrotherapy

Dentistry

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1099-MISC Equine Related Vendors

For each person in the course of your business to who you have paid the following during the year

Box 1

Rent – office space

(Not Board)

Equipment rentals

Box 3

Prizes/awards

Do not include wages, any bonuses, prizes, and awards paid to your employees. Report these on Form W-2.

Box 3

Other payments to racing partners

(for race proceeds)

Box 6

Veterinary entity payments

(ALL Vets to be included even if INCORPORATED)

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Other Reminders

Other Reminders

- 1099-MISC Due Date
  - 02/28 if paper
  - 03/31 if electronic
- 1099-NEC Due Date – 1/31/25 for both paper and electronic
- Form 1096 must accompany both as a cover for IRS submission
- DO NOT include any reimbursements
- EIN’s
  - For Single Member LLC’s, you can use the recipient’s personal name and DBA business name with a SSN
  - For Partner LLC’s, Scorp, and Ccorp, you must use EIN provided by the IRS
- 1099-K Update
  - New threshold for 2024 - $5,000

Federal Tax Incentives – Depreciation

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Bonus Depreciation

- Bonus depreciation is only available for assets placed in service before 1/1/27 and phases down as follows:
  - 60% for property placed in service during calendar year 2024
  - 40% for property placed in service during calendar year 2025
  - 20% for property placed in service during calendar year 2026

Placed in service

- Qualifying property must be purchased and placed in service in order to claim the bonus depreciation:
  - Racing prospects – when horse begins training or when horse begins racing
  - Sport horses – when horse begins training or when horse begins competing
  - Breeding stock – when the horse is available for breeding
- Examples

Bonus depreciation

- Most horse purchases now qualify; however, bonus depreciation is NOT available for the following:
  - Horses previously owned
  - Horses used predominantly outside of the U.S.
  - Horses purchased from related parties or received via inheritance or gift
  - Horses not eligible to currently be placed in service (weanlings)
  - Horses that are inventory and not placed in service

Bonus depreciation

- Other common equine assets that may qualify:
  - Equipment
  - Fencing
  - Land improvements
  - Barns
- Very helpful on farm purchases

Section 179 Expensing

- Annual limit on expensing increased to $1.22 million (2024)
- Annual phase-down threshold increased to $3.05 million (2024)
- Continues to be limited to net taxable income; not used by many horse owners for this reason
- Continues to be available only to ACTIVE trades or businesses

Depreciation: Who makes these decisions

IF HORSES OWNED VIA A PARTNERSHIP

- Depreciation decisions are made by the partnership and reflected to partners on a Schedule K1

IF HORSES OWNED VIA A CO-OWNERSHIP

- Each co-owner makes his/her own decision regarding depreciation

Federal Tax Incentives – Qualified Business Deduction

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20% qualified business deduction (Section 199A) considerations

- Reminder – this 20% deduction is only available to non-C corporate taxpayers
- Calculated at the owner, partner, or S shareholder level—K1s will provide information for each member to include with personal tax return
- The deduction amount, generally 20% of qualified business income from all businesses with limitations in certain cases, cannot exceed 20% of taxable income, excluding net capital gains

20% qualified business deduction

- Basic calculation: Individual filing a joint return has taxable income of $250,000 (no capital gains)
- Boarding and breeding business generates $300,000 of ordinary net income
- Deduction is the lesser of 20% of taxable income, which is $50,000, or 20% of qualified business income, which is $60,000
- Deduction is $50,000

20% qualified business deduction

- Same taxable income as prior example, $300,000 net income from boarding/breeding but horse racing activity generates a net loss of ($200,000)
- Deduction is the lesser of 20% of taxable income, which is $50,000, or 20% of qualified business income calculated for each business, which is $60,000 - $40,000 = $20,000
- Deduction is $20,000

20% qualified business deduction (Section 199A) considerations

- Special allocations vs. guaranteed payments
  - » Guaranteed payments are excluded from qualified business income
    - Re-work partnership agreements to replace guaranteed payments with special allocation of income items
    - Special allocation has potential to increase qualified business income deduction for partners previously receiving guaranteed payments

20% qualified business deduction (Section 199A) limitations

- Limitations may apply if 2024 taxable income exceeds the threshold ($191,951 single, $383,901 MFJ):
  - » Based on wages and/or wages and depreciable assets
  - » Specified services businesses may also not be eligible
- Complex aggregation rules beyond the scope of today’s presentation

Federal Tax Considerations

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Excess business losses

- TCJA limited business losses deductible by noncorporate taxpayers against non-business income
- Net tax losses from businesses in excess of $250,000 for individuals and $500,000 for joint filers (adjusted for inflation), are disallowed
  - » For 2023, the amounts are $305,000 (individuals) and $610,000 (joint filers)
- Excess business loss provision expires for tax years beginning after 12/31/2028

Beneficial Ownership Reporting

Beneficial Ownership Reporting overview

- Corporate Transparency Act (CTA) requires certain entities to file Beneficial Ownership Information (BOI) reports with Treasury's Financial Crimes Enforcement Network (FinCEN)
- Beneficial owners are the individuals who ultimately own or control the company, including any individual who directly or indirectly:
  - Exercises substantial control over the company; or
  - Owns or controls at least 25% of the company

BOI reporting basics

Who?	All domestic and foreign entities that have filed formation or registration documents with a U.S. state
What?	BOI report must identify the company and report the following about each beneficial owner: name, birthdate, address, and a unique identifying number from acceptable identification document
Who not?	There are 23 exceptions, including large operating entities that (1) employ more than 20 people in the U.S.; (2) had gross revenue over $5 million; and (3) have a physical office in the U.S.
When?	New entities (created/registered after 12/31/23) – must file within 30 days Existing entities – must file by 1/1/25 To change or correct previously reported information – must file within 30 days
How?	Through a secure filing system on FinCEN's website (currently in development)
What else?	Penalties apply for willful noncompliance, including (1) civil penalties up to $500/day that violation continues; and (2) criminal penalties of $10,000 fine and/or up to two years imprisonment

Hobby Loss and Passive Activity Reminders

Hobby loss reminders

- Through calendar year 2025, expenses associated with a hobby are no longer deductible
- Potentially makes the business versus hobby distinction even more important
- Accelerated depreciation increasing tax losses

Hobby loss reminders

- IRS regulation lists nine factors for determining whether or not an activity is conducted with the intent to make a profit (and, thus, a business versus a hobby)
- No single factor is determinative, but the single most important factor based on our experience and case law is maintenance of good books and records followed by development, evaluation, and adjustment of operations to achieve profit potential
- Generating profit in two out of seven years and what it means

Active participation

- Applicable to business activities
- May affect the timing of tax losses generated
- Most common level of participation by horse and farm owners is 500 hours per year in order to be treated as active
- Qualifying activities for horse and farm owners

Looking Forward… Expiring TCJA Provisions and Potential Election Impact

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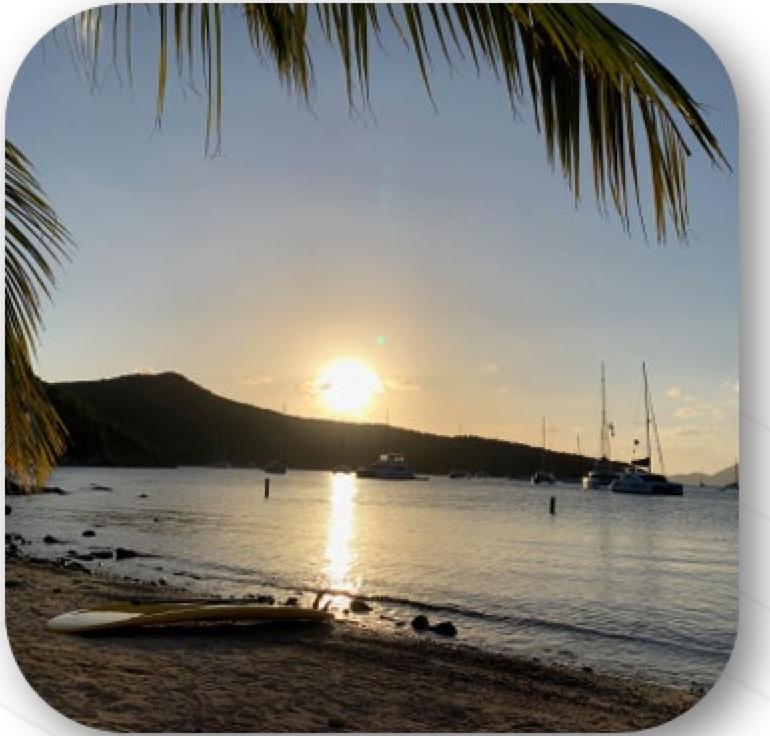
Watching the sunset



- The TCJA of 2017 was the most significant overhaul of the federal tax code since 1986
- Without Congressional action, many provisions will sunset after December 31, 2025

Key provisions expiring after 12/31/2025

Income Tax Provisions	Description
Individual income tax rates	The TCJA reduced the individual income tax rates, including dropping the top rate from 39.6% to 37%. The rates revert to pre-TCJA amounts for tax years beginning after 12/31/2025.
Increased standard deduction	The TCJA doubled the standard deduction for all filing statuses. The increased standard deduction expires for tax years beginning after 12/31/2025.
Suspension of miscellaneous itemized deductions	The TCJA suspended miscellaneous itemized deductions subject to the 2% floor. The suspension expires for tax years beginning after 12/31/2025.
Cap on state and local tax (SALT) deduction	The TCJA capped the SALT deduction at $10,000. The cap expires for tax years beginning after 12/31/2025.
Increased AGI limit on charitable contributions	The TCJA increased the AGI limit on cash contributions from 50% to 60%. The increased limit expires for tax years beginning after 12/31/2025.
Qualified business income (QBI) deduction	The QBI deduction applicable to owners of pass-through entities expires for tax years beginning after 12/31/2025.

Phase-down of bonus depreciation

Placed in Service Date	Bonus Depreciation Percentage
After 9/27/2017 and before 1/1/2023	100%
After 12/31/2022 and before 1/1/2024	80%
★ After 12/31/2023 and before 1/1/2025	60%
After 12/31/2024 and before 1/1/2026	40%
After 12/31/2025 and before 1/1/2027	20%

Expiring estate and gift tax provisions

- The following amounts will decrease from an inflation-adjusted $10 million to $5 million after 12/31/2025
  - » Estate and gift tax unified credit basic exclusion
  - » The Generation-Skipping Transfer (GST) tax exemption

Year-End Tax Planning

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Projecting financial and taxable activity

- Track year-to-date results to evaluate if tax planning is needed
- Gather W-9s from vendors to assist with Form 1099 reporting

Increasing tax income

- Consider election out of the favorable bonus depreciation – may be done on an asset class-by-class basis

Reducing taxable income

- Most equine industry participants qualify to use cash basis reporting for US income tax reporting
- There should be a non-tax reason for prepayments of expenses (for example, discounts or access to a particular horse)
- Consider electing installment sale treatment if not all sales proceeds are due by year-end (but beware of the depreciation recapture)

Donation of horses

- May receive a charitable deduction for the fair market value of the horse donated to charity (subject to certain limitations)
- Gift must be made to a 501(c)(3) charity and be unconditional
- Proper documentation must be obtained – substantiation documents and a qualified appraisal by a qualified appraiser of the fair market value of the horse exceeds $5,000

Donation of horses - limitations

- The fair market value of the donated horse must be reduced by the amount of gain on a sale that would be ordinary income if the horse were sold at fair value.
  - » The charitable deduction for horses held as inventory (pinhooked) or owned 24 months or less is limited to tax basis
  - » The charitable deduction for horses owned more than 24 months on which depreciation has been claimed is reduced by the amount of depreciation claimed

Donation of horses - limitations

- If the charity does not use the horse to further its charitable purpose, then the charitable deduction is limited to the tax basis of the horse
- Consider alternatives for the horse which may be more income tax efficient

Questions?

Thank you

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