¶435 Depreciation of Farm Property

NEW LAW EXPLAINED

Farming machinery depreciated over five years; 200 percent DB method allowed; ADS required if farming business elects out of interest deduction limits.— Modifications to the treatment of certain farm equipment include:

- a decrease in the 7-year recovery period for new farming machinery and equipment to 5 years, and
- elimination of the rule requiring use of the 150-percent-declining balance method on property used in a farming business.

Five-year recovery period for new farming machinery and equipment. Effective for property placed in service after December 31, 2017, a 5-year recovery period applies to any machinery or equipment (other than any grain bin, cotton ginning asset, fence, or other land improvement) used in a farming business if the original use commences with the taxpayer after December 31, 2017 (Code Sec. 168(e)(3)(B)(vii), as amended by the Tax Cuts and Jobs Act). Generally, a seven-year recovery period previously applied to this property (Rev. Proc. 87-56, Asset Class 01.1).

CAUTION

The provision only applies to new machinery and equipment used in a farming business. A 7-year recovery period continues to apply to used farming machinery and equipment.

200-percent declining method allowed for farming property. The provision that requires MACRS 3-, 5-, 7-, and 10-year property placed in service after 1988 and used in a farming business to be depreciated using the 150-percent declining balance (DB) method in place of the normally applicable 200 percent DB method is repealed, effective for property placed in service after December 31, 2017 (Code Sec. 168(b)(2)(B), as stricken by the 2017 Tax Cuts Act).

COMMENT

A taxpayer may now elect to depreciate any class of 3-, 5-, 7-, or 10-year farming property using the 150-percent declining balance method, the straight-line method, or the alternative depreciation system (ADS) (Code Sec. 168(b)(2)(D)). The election was not previously available because such property had to be depreciated using the 150-percent declining balance method.

Farming business defined. As defined in Code Sec. 263A(e)(4) and Reg. §1.263A-4(a)(4), the term "farming business" means a trade or business involving the cultivation of land or the raising or harvesting of any agricultural or horticultural commodity (e.g., the trade or business of operating a nursery or sod farm; the raising or harvesting of trees bearing fruit, nuts, or other crops; the raising of ornamental trees (other than evergreen trees that are more than six years old at the time they are severed from their roots); and the raising, shearing, feeding, caring for, training, and management of animals). A farming business includes processing activities that are normally incident to the growing, raising, or harvesting of agricultural or horticultural products. A farming business does not include contract harvesting of an agricultural or horticultural commodity grown or raised by another taxpayer, or merely buying and reselling plants or animals grown or raised by another taxpayer.

Farming business electing out of interest deduction limitation must use ADS for property with recovery period of 10 years or greater. Any property with a recovery period of 10 years or greater which is held by an "electing farming business" that makes an election out of the new rules which disallow the deduction for net interest expense in excess of 30 percent of the business' adjusted taxable income must be depreciated using the MACRS alternative depreciation system (ADS) (Code Sec. 168(g)(1)(G), as added by the 2017 Tax Cuts Act). See ¶510 for discussion of 30 percent limitation on business interest expense deductions.

COMMENT

Under ADS, the straight-line method applies using a recovery period that is usually longer than the regular recovery period. The ADS recovery period is the asset's class life, usually as shown in Rev. Proc. 86-56.

An electing farming business is a farming business as defined above that elects out of the interest deduction limitation or any trade or business of a "specified agricultural or horticultural cooperative" (as defined in new Code Sec. 199A(g)(2)) with respect to which the cooperative makes an election out of the interest deduction limitation (Code Sec. 167(j)(7), as added by the 2017 Tax Cuts and Jobs Act).

A specified agricultural or horticultural cooperative is an organization to which part I of subchapter T applies, and which is engaged in—

1) the manufacturing, production, growth, or extraction in whole or significant part of any agricultural or horticultural product;

2) the marketing of agricultural or horticultural products which its patrons have so manufactured, produced, grown, or extracted; or

3) the provision of supplies, equipment, or services to farmers or to organizations in items (1) or (2) (Code Sec. 199A(g), as added by the 2017 Tax Cuts Act).

Effective date. The amendments made by this section reducing the recovery period of farm machinery and allowing use of the 200-percent declining method apply to property placed in service after December 31, 2017 (Act Sec. 13203(c) of the Tax Cuts and Jobs Act). The amendment requiring an electing farming business to use ADS to depreciate property with a recovery period of 10 years or greater applies to tax years beginning after December 31, 2017 (Act Sec. 13205(b) of the 2017 Tax Cuts Act).