

A Case for Land Contracts

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Many of the newspaper, magazine, and online articles that have circulated for the last few months have related to the Coronavirus and how it has affected or is going to affect how business is conducted moving forward. When looking at the farmland market, however, the double whammy of an increased supply and drop in demand for oil has created a corresponding drop with ethanol usage and commodity prices that will be more disruptive than the Coronavirus. Although the land market still has several ready, willing, and able Buyers that have the financial ability to write a check for land, there are situations where a cash sale to the landowners isn't in the best interest of a Seller. Those of us that make a living through land brokerage and auctions as well as farm and land management will need to seek creative solutions for landowners where that is not the case.

An example of a creative solution or rather deal structure that proved beneficial to both the Buyer and the Seller was a recent transaction for a farm in Guthrie County, Iowa. The landowner couple decided that they wanted to sell their farmland property but soon realized the lower basis in their farmland was going to create a major capital gains tax ramification for them. A way for them to reduce their tax exposure was through a

land contract or in other terms “Seller Financing”. This would allow for capital gains to be paid only on the principal portion of the payment every year versus if they were to sell the property and receive a lump sum. The couple did sell one of their three farmland tracts to a neighboring landowner with the principal balance being paid to them in equal payments over 3 years.

The landowner remained committed to the sale of their remaining farmland but the more principal that is received each year equates to more capital gains taxes paid. Also, the landowner couple’s tax status was “Married filing Jointly” and with Federal capital gains rates thresholds at 0% from \$0 to \$78,750, 15% for capital gains \$78,751 to \$488,850, and 20% for more than \$488,850; we wanted to limit their taxable amount as much as we could. Instead of a traditional principal and interest contract, we structured a deal with a local landowner / farmer for an interest only contract for 3 years. After the interest only period, the landowner receives a lump sum principal payment and the balance of the sales price being paid over a 15-year contract with principal and interest payments. This might appear overly complicated but the layman’s terms of what was accomplished was that a husband and wife realized the sale of their farmland with terms that allowed the sales price to be maximized all while the primary goal of limiting the landowners annual capital gain rates and amounts. The concept of a contract sale is not new, but our limited understanding of the current tax code allowed a beneficial result for the landowner. The Sellers attorney and accountant were apprised of all details and proved to be valuable resources.

Peoples Company, myself, and our agents welcome an opportunity to visit with you about your situation and how we might be able to advise you. Peoples Company agents pride themselves in the ability to not only be premier marketers of farmland, but serve as consultants for the varying circumstances each landowner might find themselves in.