IOWA STATE UNIVERSITY
Center for Agricultural Law and Taxation

Legal Issues Brief

New Iowa Tax Law Benefits Retired Farmers

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OVERVIEW

On March 1, 2022, Governor Kim Reynolds signed HF 2317 into law. The new tax law will reduce individual and corporate income tax rates, provide exemptions from Iowa tax for most forms of retirement income--including retired farmer rental income--and scale back certain tax credits. These changes have different effective dates, but most changes will begin phasing in during the 2023 tax year.

RETIREMENT INCOME TAX EXEMPTION

Beginning in 2023, the new law modifies Iowa Code § 422.5(3)(a) to exempt from Iowa taxation all "retirement income" for those who are disabled or 55 years of age or older. It also exempts retirement income received by surviving spouses. Current law exempts retirement income only in an amount up to $6,000 for singles, and $12,000 for those who are married filing jointly. The new law does not change the full income exclusion for military retirement benefits paid by the federal government at any age.

Retirement income includes pension plans, defined benefit or defined contributions plans, annuities, individual retirement accounts, plans maintained or contributed to by an employer, or maintained or contributed to by a self-employed person as an employer, and deferred compensation plans or any earnings attributable to the deferred compensation plans.

FARM LEASE INCOME EXCLUSION

Recognizing that for many farmers, their land is their retirement account, the new law allows an eligible retired farmer-lessor to elect to exclude from Iowa income taxation the net income received under a written farm lease covering real property. To be eligible for this election (beginning in 2023), the lessor must meet all of the following requirements:

- Be disabled or 55 years of age or older
- No longer be materially participating in the farming business
- Owned the real property and materially participated in a farming business for 10 or more years

The exclusion applies only to income from **written** farm tenancy agreements, including cash leases, crop share leases, and livestock share leases. The law does not apply to rental income received as an owner of an entity taxed as a partnership, an S corporation, or a trust or estate, even if the net income passes through to the eligible individual.

> **Note**: This provision would appear to allow the exclusion to apply to income from land owned by a single-member LLC, but not to income from land held by an LLC taxed as a partnership (i.e. an LLC comprising only spouses).

Individuals who make an election under this section **may not**:

- Apply the Iowa capital gain deduction in the current or succeeding tax years
- Take the beginning farmer tax credit in the current or succeeding tax years

IOWA CAPITAL GAIN DEDUCTION

The law also modifies the Iowa capital gain deduction. The current Iowa capital gain deduction allows many taxpayer who sell businesses or certain livestock to avoid Iowa tax on the sale. In 2023, this deduction changes significantly to apply only to the sale of real property used in a farming business and to the sale of some draft, dairy, and breeding livestock by retired farmers.

Deduction for Some Real Property

Beginning in 2023, a seller of real property used in a farming business may qualify for the Iowa capital deduction in two different ways.

Option One:

- The seller materially participated in a farming business for 10 years (for retired or disabled farmers, the 10 years is considered in the aggregate) and
- The seller held the property used in a farming business for a minimum of 10 years

If the seller meets the material participation and holding requirements, there is no requirement that the buyer and the seller are related.

Option Two:

- The seller sells property held and used in a farming business to a relative, including lineal descendants and second degree relatives.

If the buyer of the property is a qualifying relative, the seller is not required to meet material participation or holding period requirements.

Deduction for Some Livestock

Beginning in 2023, the new law also allows retired or disabled farmers (55 years of age or older) to elect to deduct gain from the sale of breeding, draft, dairy or sport cattle or horses (held for 24 months or more) if the taxpayer:

- Materially participated in the farming business for five of the eight years preceding retirement or disability, and
- Sold all or substantially all of the taxpayer's interest in the farming business when the election is made.

The same rule will apply to the sale of other breeding livestock held for a period of 12 months or more.

Special Rules for Retired Farmers

Retired farmers may make a single lifetime election to exclude all qualifying capital gains from the sale of real property used a farming business and/or eligible livestock.

Retired farmers who elect to exclude gain under this provision, however, may not claim the Iowa beginning farmer tax credit. They are also ineligible to exclude farm rental income from Iowa taxation.

RETIRED FARMERS MUST CHOOSE

Beginning in 2023, the new Iowa law requires retired farmers to elect between (1) excluding eligible farm rental income or (2) excluding eligible capital gain from Iowa taxation. Once they make an election, it may not be changed. A retired farmer who has excluded farm rental income from Iowa taxation, for example, may not ever take the Iowa capital gain deduction. Retired farmers should discuss this election with a trusted tax professional.

NO IMPACT ON FEDERAL TAX LIABILITY

The provisions discussed in this brief apply only to Iowa tax liability. No law excludes farm rental income or capital gain from federal taxation.