EXTENSION

AGRICULTURE

Crowd Funding?

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Include Tax Planning into Your Project!

There is a lot of excitement about crowd funding these days. Rightfully so, most people get excited about the prospect of free money. But is this money free? What do we call this money? Is it a gift, a donation, a pledge, taxable income, WAIT…..did someone say taxes? Amidst all the excitement it appears that there is still uncertainty about the tax implications of your next crowd funding campaign. Let’s look at a few of these issues now so that no one will be totally surprised when it comes time to file your farm business return. We expect to learn more as 2012 progresses, so watch out for future posts and updated information.

Step 1: Find a trusted tax advisor

We don’t have all the answers on how the IRS or Vermont Department of Taxes will view crowd funded proceeds at the close of the 2012 tax year. These situations are likely to require professional support.

Issue 1: Taxable Income

Contact with a few accountants this month confirms that if a commercial business receives donations it is considered taxable income. Many crowd funding campaigns are also rewarding the donors with actual products from the business. This transaction is easily interpreted as a “sale”. Again, this is taxable income.

Issue 2: Gift Status

The IRS and the VT Department of Taxes have different laws related to gifts. If future interpretation of a crowd funded pledge defines the proceeds as gifts, then the VT 2011 Income Tax Return Booklet (http://www.state.vt.us/tax/index.shtml) states on page 52 and 53 that there is an exclusion for the FIRST $6,500 in gifts, but the total amount of gifts exceeding $6,500 is considered taxable income. IRS gift and tax definitions are different. Look them up here: http://www.irs.gov/

Issue 3: Deductible Expenses vs. Capital Depreciation

Farmers can refer to IRS Publication 225 to understand which annual expenses are deductible (http://www.irs.gov/pub/irs-pdf/p225.pdf). In general, annual operating expenses are deductible and will offset any crowd funded income. Example: $5,000 received less $5,000 in operating expenses equals $0 in taxable net income. If your proceeds are being put into capital investments (equipment, property or improvements with over 1 year lifespan) then these items need to be depreciated. While several depreciation formulas can be applied to a new investment, in many cases the first years depreciation will not equal the actual cash outlay for the purchase of the asset. This is likely to result in taxable income. Example: $5,000 received and $5,000 in cash payment for asset, but depreciation calculation equals $1,750 in year one. $5,000 less $1,750 equals $3,250 in taxable income.

Issue 4: Unspent Funds at Year End

If we assume that crowd funded proceeds continue to be defined as taxable income then owners need to plan what time in the year they will accept the proceeds in relation to how they will spend the funds. If proceeds are deposited on December 15 the business may not be able to execute all the offsetting expenses by year end. The balance of funds will be taxable so plan ahead!

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