RURAL TAX EDUCATION

RTE/2021-01

March 2021 RuralTax.org

Tax Issues Related to Debt Relief of Socially Disadvantaged Producers*

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The American Rescue Plan Act of 2021, H.R. 1319, was signed into law on March 11, 2021. The bill included the following provision "*The Secretary shall provide a payment in an amount up to 120 percent of the outstanding indebtedness of each socially disadvantaged farmer or rancher as of January 1, 2021, to pay off the loan directly or to the socially disadvantaged farmer or rancher (or a combination of both*)," found in Section 1005(a)(2) on page 9 of the bill.

Details of how and when this will be carried out are not yet known and additional decisions may affect the tax treatment of the payments. This article relies heavily on how previous debt relief programs were undertaken. The purpose here is to highlight some of the issues that could affect the taxation issue around payments for debt relief. As more details become known, we will address them in future publications. **This information is intended for educational purposes only. Seek the advice of your tax professional regarding the application of these general principles to your individual circumstances.**

Items to Consider

Here are a few issues to consider.

- **Recipients will need to file a tax return to comply with IRS regulations.** All recipients will need to file a federal income tax return reporting this payment as income, regardless of their current income level, land status, current employment status, and even if they have not filed an income tax return before. Failure to file a return with the correct income included could result in additional amounts owed to the IRS for interest and penalties.

* **The information reflects the views of the author(s) and has not been sanctioned by the Internal Revenue Service.**

- The provision included payments of an amount up to 120% of the outstanding indebtedness. The intent behind an additional amount above 100% is most likely intended to account for the tax consequences of the payment. The actual tax liability will depend on the individual's tax situation. For some, this may be less than the tax owed, but for others it may be more. We will be updating this material as new information concerning the income tax reporting becomes available.

- In addition to the federal tax liability, individuals may also have a state and local tax liability for the payments. Once program details are known, recipients should consult with their tax professional about the potential tax liability for state and local taxes.

- The settlement may have implications on other tax provisions as well. It may affect the earned income credit, child care credit, and tax on social security benefits.
