Excess Fertilizer Supply Deduction

Tax Savings Hidden in Your Soil

Agricultural landowners can unlock significant tax savings through an IRS provision that recognizes the value of residual soil nutrients at the time of purchase or inheritance. This guide outlines which properties qualify, how nutrient value is assessed, and the steps required to document and claim the deduction.

The IRS tax code provides a powerful but often overlooked opportunity for agricultural landowners: the ability to deduct the value of residual soil nutrients present at the time of purchase or inheritance. By capturing this deduction, landowners can not only reduce taxable income but also improve the financial performance of farmland and ranchland investments. On average, deductions amount to approximately $1,700 per acre, though the actual benefit varies based on soil conditions, cropping history, and documentation.

WHAT LAND QUALIFIES?

Crop, ranch, or pastureland that was purchased or inherited with a step-up in basis after January 1960, and is in agricultural production during the amortization period of the Excess Fertilizer Supply Deduction, can qualify for this deduction. Because land and nutrient values have changed significantly since 1960, property purchased or inherited in 2010 or later typically provides the greatest economic benefit.

Land that is covered by Conservation Easements that allow for agricultural production can also qualify, while land enrolled in crop Conservation Reserve Programs cannot.

HOW IS THE VALUE DETERMINED WHEN HINDCASTING OR IF THERE IS A GAP BETWEEN THE PURCHASE OF THE PROPERTY AND SOIL SAMPLING?

If hindcasting is performed, or if there is a time gap between purchase and soil sampling, analysts will need records of fertility applications and crop production during that period to account for any changes in nutrient levels. For ranchland, this typically includes grazing records such as stocking rates, stocking densities, and any fertilizer applications (if applicable).

This information is used to measure the build-up or draw-down of nutrients over time. A qualified third party then uses this information to adjust the results of current soil tests, ensuring an accurate estimate of the nutrient levels at the time the property was purchased or inherited.

WHEN CAN YOU DEDUCT THE EXCESS FERTILIZER SUPPLY?

Some farmers and ranchers are able to claim up to 100% of the Excess Fertilizer Supply Deduction in the year of filing, while others may need to spread the deduction over several years. Clients tend to choose amortization periods of 3 to 7 years, depending on their situation. As a guideline, we generally recommend an aggregate deduction of no more than 50% to 75% of the purchase price of the farmland or ranchland.

WHAT ARE THE POTENTIAL TAX SAVINGS?

The value of the deduction depends on your tax bracket. For example, if the excess fertilizer is valued at $1,700 per acre:

Deduction/Acre	Cost/Acre	Tax Bracket	Cash Savings on Taxes	Multiple on Invested Capital
$1,700	$40	10%	$170	4.25
$1,700	$40	20%	$340	8.5
$1,700	$40	30%	$510	12.75
$1,700	$40	40%	$680	17

Cost/Acre – The estimated fee charged by a qualified third-party provider for data collection, analysis, and reporting needed to calculate and document the excess fertilizer value per acre.

HOW HAS THE IRS VIEWED THIS DEDUCTION?

Two significant IRS authorities outline how agricultural landowners can benefit from the Excess Fertilizer Supply Deduction: Private Letter Ruling 9211007 (PLR) and the Market Segment Specialization Program Training 3149-122 (MSSP).

The PLR sets out four key criteria for land owners to amortize the cost of fertilizer acquired with the land:

1. Establish the presence and extent of the fertilizer.
2. Show the level of soil fertility attributable to fertilizer applied by the previous owner.
3. Provide a basis to measure the increase in fertility in the land.
4. Evidence indicating the period over which the fertility attributable to the residual fertilizer will be exhausted.

The MSSP, issued in July 1995, reinforces these requirements and further states that landowners must prove beneficial ownership of the residual fertilizer supply. This means maintaining comprehensive documentation, including soil tests and supporting analytics, to quantify the amount of fertilizer present at the time of purchase or inheritance.

WHO HANDLES AN IRS AUDIT IF ONE OCCURS?

An audit covers all your tax returns and is managed by your Certified Public Accountant (CPA). A qualified third-party group will support the audit process by helping the auditor review and understand their methodologies, reporting, and results.

WHAT HAS BEEN THE SUCCESS RATE IN IRS AUDITS?

Boa Safra, a qualified third-party group that SEK partners with, has maintained a 100% success rate in audits. To date, they have worked through several audits with deduction values ranging from tens of thousands to millions of dollars. All reports have been accepted without adjustments.

HOW HAVE THE VARIOUS STATES VIEWED THIS DEDUCTION?

While some states have shown a greater tendency to challenge how the deduction is calculated, there is no documentation indicating that any state disallows the deduction or requires it to be recalculated under different state-specific criteria.

HOW DOES THE ALLOCATION OF THE PURCHASE PRICE AFFECT INCOME TAX FOR THE SELLER OR FUTURE SALE OF THE QUALIFIED LAND?

If part of the purchase price is allocated to fertilizer or other farm-related assets, the seller generally recognizes ordinary income, which is taxed at a higher rate than capital gains. In addition, when the property is later sold, any portion of the purchase price allocated to the Excess Fertilizer Supply Deduction would be subject to Section 1245 recapture and taxed at ordinary income rates.

EXAMPLE #1

- Farmer Bob bought 160 acres of ground in 2015 and plans to use Form 3115 to deduct the Excess Fertilizer Supply Deductions that were missed from the time of purchase or inheritance.
- Bob did not have soil testing at the time of purchase in 2015. However, Bob has records of what he has applied to his farm from time of purchase until present day, and he also has all of his crop production data for each of those intervening years (a standard among all farmers today).
- In this case, Bob has grown corn-on-corn for the last 9 years, and his average yield has been 200 bushels per acre.
- The qualified third-party group will soil test the 160 acres in 2024 and will analyze all available Macro and Micronutrients in the top 6.75 inches of the soil.
- The qualified third-party group will take the nutrient load analysis and compare it to what has been applied on the farm for each of those intervening years. In this case, Farmer Bob applied fertilizer to grow 220 BPA corn each year.
- Bob deducted his fertilizer applied each year to his farm on his Schedule F as an ordinary business expense.
- The qualified third-party group will take the current soil test data, crop production history, and annual fertilizer applications to hindcast what the Excess Fertilizer Supply Deduction would have been in 2015.
- The qualified third-party group will apply a discount factor to account for the excess nutrients Bob applied, since his annual applications for 220 bushels per acre exceeded the crop removal of 200 bushels per acre. This ensures no double deductions occur between the Excess Fertilizer Supply Deduction and ordinary Schedule F deductions.
- This is a scientific and agronomic way to compute the Excess Fertilizer Supply Deduction.

EXAMPLE #2

- Rancher Bob bought 640 acres of ranching/cow-calf ground in 2015 and plans to use Form 3115 to deduct the Excess Fertilizer Supply Deductions that were missed from the time of purchase or inheritance.
- Bob did not have soil testing at the time of purchase in 2015. However, he has not applied any fertility to his ranch from the time of purchase until the present day.
- Bob has raised cattle and hay/grass for the last 9 years.
- The qualified third-party group will soil test the 640 acres in 2024 and analyze all available Macro and Micronutrients in the top 6.75 inches of the soil.
- Bob would have deducted any fertilizer he applied each year on the ranch from his Schedule F as an ordinary business expense (in this case, no fertilizer was applied).
- The qualified third-party group will take the current soil test data and run an Excess Fertilizer Supply Deduction calculation. The current-year deduction will be much lower than it would have been in 2015 at the time of purchase, because the ranchland has been producing cattle and hay/grass without new fertilizer applications.
- This is a scientific and agronomic way to compute the Excess Fertilizer Supply Deduction.

Guidance for Your Unique Situation

Taking advantage of the Excess Fertilizer Supply Deduction can deliver meaningful tax savings while strengthening the value of your agricultural investment. By working with experienced advisors and qualified third parties, you can ensure the deduction is calculated correctly and fully supported for long-term benefit.

If you have questions or believe you may qualify – whether for an upcoming or previously purchased property – please contact us. Our agribusiness team is here to provide expert guidance and tailored solutions to ensure compliance, maximize your resources, and support your unique situation.

Ryan Leppo, CPA, MBA
Member of the Firm
Chambersburg, PA
717.263.3910
rleppo@sek.com

Denver Martin, CPA
Member of the Firm
Hagerstown, MD
301.733.5020
dmartin@sek.com

Nick Chapman
Manager
Hagerstown, MD
301.733.5020
nchapman@sek.com

Bradley Kearns, CPA
Member of the Firm
Chambersburg, PA
717.263.3910
bkearns@sek.com

Aaron Althouse, CPA
Manager
York, PA
717.900.2021
aalthouse@sek.com

Darian Hufcut, EA, MAcc
Senior Associate
Chambersburg, PA
717.263.3910
dhufcut@sek.com

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Guidance You
Can Count On.

Source: Boa Safra