

Residual Fertilizer Deduction

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Why This Issue is Occuring?

- IRS Guidance: A farmer may allocate a portion of the purchase price for a piece of land to residual fertility in the soil (prior unused amounts)
- The claim is that the residual fertilizer increased the cost
- Valuing the residual fertilizer lowers the cost of the property and provides a tax deduction
- If no value is placed on the residual fertilizer, this cost is locked into the property's tax basis (no benefit until the land is sold)

What is Happening?

- Companies are contacting farmers and providing the following:
- A tax break exists that you may qualify for.
- “If you have purchased or inherited farmland within the last 15 to 20 years, you may qualify for tax deductions based on residual nutrients found on your farm or ranch.”
- “Our clients’ nutrient loads are over \$1,300 per acre, resulting in significant tax savings when they work with us.”
- Some companies are stating that this process can also apply to pasture (improved pastures and native range)

The Issue

- A 1992 Technical Advice Memorandum (TAM 9211007)
- Requirements for a farmer to amortize the residual fertility
 - Establish the presence and extent of the fertilizer;
 - Show the level of soil fertility attributable to fertilizer applied by the previous owner;
 - Provide a basis upon which to measure the increase of fertility in the soil; and
 - Provide evidence indicating the period over which the fertility attributable to the residual fertilizer will be exhausted.
 - Show the decline of the residual fertilizer supply.

TAM 9211007 Suggests

Under the *right set of facts*, the IRS will allow a purchaser of land to allocate part of the purchase price to the residual fertilizer supply acquired with the land and amortize that cost over the period the fertility attributable to that residual fertilizer will be exhausted.

- Beneficial Ownership
- Presence and Extent of Fertilizer
- Level of Fertilizer Attributed to Previous Owner
- Basis to Measure the Increase (there must be no incentive to “over fertilize”)
- Period of Exhaustion of Residual Fertility

Problems with Promoter Points

- Farmers can retroactively take a deduction on purchased or inherited land from 15 to 20 years ago with out soil tests
- Not only P and K are valued, but also micronutrients (which are to be hard to place a value on)
- As pay for their services, they want a significant portion of the tax savings, but these companies will not file the return (costs \$40 / acre or more for the service of determining residual)
- They do not fully understand the Tax Code (IRC Section 180)

The Risks

- If the IRS challenges a position taken on a return,
 - it may assess a 20 to 40% penalty against the underpayment of tax, and
 - up to a 75% penalty for civil fraud
- State penalties can accrue too.

If a Farmer Wants to Use This Provision

- Pay for expert analysis to prove that the soil at issue has nutrient levels in excess of standard or baseline levels.
- Demonstrate through soil experts that the excess fertility has a useful life that is depleting or being exhausted over a certain period of time (generally two to seven years).
- Be consistent in the approach. Taking a deduction for excess fertility must be reflected in the amount of fertilizer applied in the year of the deduction.
- Be diligent in reviewing and submitting data provided by these consultants.

What about Extension?

- Companies have been and are contacting county educators in Oklahoma and other states seeking hosts for meetings.
- What should you do?
- I have visited with OSU administration and it is strongly urged that you avoid assisting these promoters.
- I personally feel that we do not want to be involved in this.
- There is a strong potential for abuse and the farmer (taxpayer) may pay the ultimate price (IRS Audit and potential penalties)

What About Extension

- If you are contacted by a promoter:
 - I would strongly urge you to not host any of these programs.
 - What and how they are promoting this is not always 100 percent accurate.
 - When a farmer contacts you, please contact me if you are uncomfortable with providing information.
- There is a lot of confusion being created with the issue of “residual fertility”.

Survey and Contact Information

Link to webinar survey

https://okstatecasnr.az1.qualtrics.com/jfe/form/SV_8vHELAXAYxYe6BU

Questions and Comments

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The End!
