JOHN DEERE CREDIT

Tax Benefits

At a Glance

When it comes to taxes, there are two main subjects to be concerned with: tax liability (the amount you pay) and common IRS penalties. The way you finance your equipment, for instance, can have a major impact on how much money you pay the government. This sheet will help you determine which options have the best tax advantages.

A Closer Look

Q. *Naturally, I want to minimize my tax liability. What steps should I take?*

A. If you've been buying your equipment, you're already familiar with the concept of depreciation (taking a tax deduction for equipment's loss in value over the years). Some leases allow you to expense 100% of your payments. Both these options enable you to reduce your tax liability. The more you depreciate or deduct, the lower your reported income, and the less tax you pay.

Q. *Which is better?*

A. That depends on the specifics of the transaction, and where your home office is located.

Q. *What difference does it make where I'm located?*

A. Most states charge a use tax on leases and a sales tax on loans.

Q. *Does it always work out in favor of a lease?*

A. Not always. It depends on the specifics of the loan, the lease, and the situation. It's always a good idea to check out all your options. If you're looking for ways to lower your tax liability, a lease might be just the thing.

Q. *What if I sell the equipment outright instead of trading it in?*

A. That's a whole different situation. If you sell a piece of equipment, you pay tax on the gain—the difference between the sales price and the tax value. This is true regardless of how you originally paid for the equipment—loan, lease, or cash.

Q. *What about tax consequences?*

A. It's common for contractors to accidentally find themselves in one of these inconvenient tax situations.

Alternative Minimum Tax (AMT)

This is a common penalty that can easily be avoided. Businesses are required to pay a minimum tax. A business can have so many deductions (depreciation being a major one), that the business does not meet the minimum IRS tax requirement. When this happens, the IRS recalculates the amount of tax you owe, triggering the alternative minimum tax, or AMT. The AMT generally eliminates most tax deductions, and recalculates the amount of tax due based on a higher number. The business will then be required to pay whichever tax due amount is higher. If you pay the AMT, you'll receive a credit that can be used in future years, whenever your AMT falls below your regular taxable income. This credit never expires.

Mid-Quarter Convention

This IRS rule states that if you acquire more than 40% of your equipment (for the current year) in the fourth quarter of the taxable year, you're subject to a substantial penalty—not only on the fourth quarter purchase, but on all the equipment you purchased throughout the year. This penalty has a direct impact on how much you can depreciate. Generally, it reduces the amount substantially. Because you now owe more tax, this has an immediate, negative effect on your cash flow.

Q. *How can I avoid these consequences?*

A. In both cases, leasing may be the answer. You can avoid the AMT by acquiring equipment under an operating lease, so you can expense the payments instead of depreciating the equipment. And, because mid-quarter convention is based on recalculating depreciation, it may be in your best interest to lease fourth-quarter equipment. The most important thing you can do, however, is talk to a qualified accountant—one who understands these constantly changing tax laws and regulations.

(continued)

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Don't pay more than you have to.

Taxes are a constant challenge for contractors. You can't avoid them entirely, but if you plan properly you can avoid paying more than you have to. Leasing offers a number of substantial tax advantages, so make sure your John Deere dealer knows you're interested in this beneficial option.

Always discuss your equipment acquisition plans with a qualified accountant.

The information on this sheet is intended only for your general illustration purposes, and is not offered as legal, tax, or accounting advice. This information does not consider taxes, depreciation, the half-year convention, expensing the lease payments, interest deductions, etc. Loan rates, lease charges, and residual values vary based on structure and creditworthiness.

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