

An Introduction to Ag Taxes: What New Farmers Should Know

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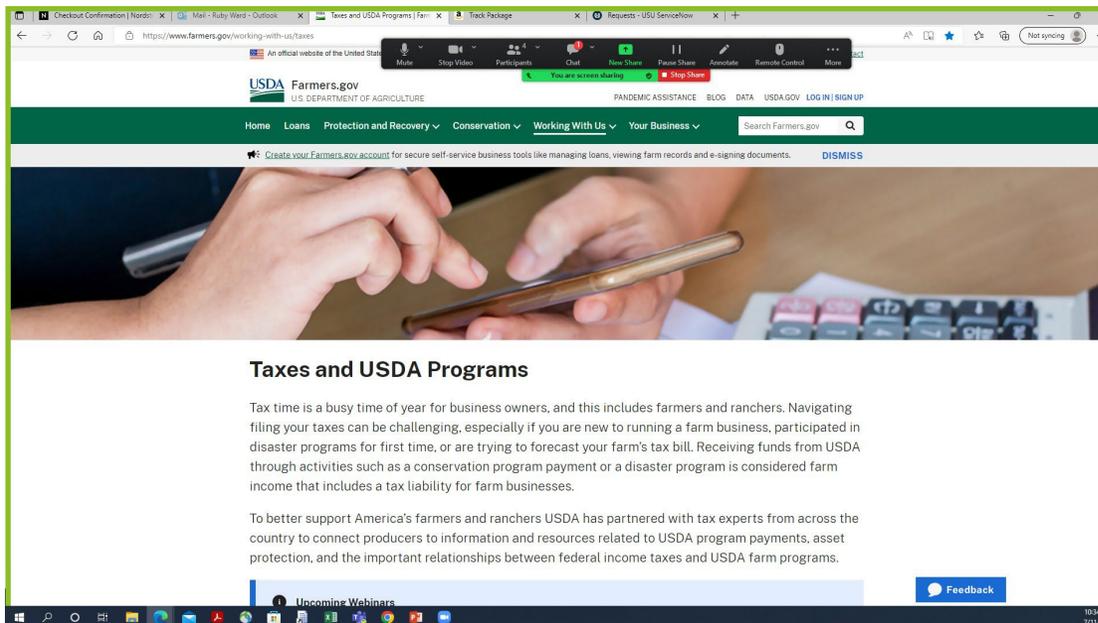
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Tax and Financial Education Project

- 3-Year USDA-FSA Funded Project
- Tax related educational materials:
 - Beginning Farmers/Ranchers
 - Commercial Farmers/Ranchers
 - Socially Disadvantaged Farmers/Ranchers
 - Landowners
 - Others



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- Website hosted by Utah State University
- Material developed, managed, and owned by the **National Farm Income Tax Committee**
- Informational Material on Ag, Timber, and Rural tax topics include but not limited to:
 - Disaster/Weather Losses
 - Treatment of Government Payments
 - Farm Losses and Hobby Rules
 - Self-Employment Taxes
 - Estate and Gift Taxes
 - Like Kind Exchanges
 - Depreciation
 - Etc...

Program Agenda

- Who is a farmer for tax purposes?
- Choosing a tax professional



New Farmer Tax Topics

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Note: Fact sheets on both topics are available on RuralTax.org/newfarmertax

Farm vs. non-farm

- **Farm** income and expense is reported on **Schedule F**
- **Business** income for a non-farm business is reported on **Schedule C**.
- Someone not classified as a farmer may still be engaged in farming activities and have farm income.



Farm vs. Non-Farm Examples

- Bob raises wheat and sells his wheat to the local elevator.
- Rosa has a flock of milking goats and sells the milk to a local organic foods co-op.
- Amal grows cut flowers which she sells weekly at the local farmer's market.
- Ricardo raises lettuce and cabbage which he sells to a salad processing company.
- Louisa operates a cattle ranch; she sells weaned calves to a feedlot investor.



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- Producer raising or growing a product and selling that product.
- They have not further processed or modified the product.

Farm vs. Non-Farm

- Business could be split between farm and non-farm.
 - Vineyard and winery
 - Production of grapes (Farm income – reported on Schedule F)
 - Sale of Wine, Juice, or Jelly (Non-farm income – reported on Schedule C)
 - Apple Orchard or a Pumpkin Patch
 - Sale of apples or pumpkins that have not been processed is farm income (Schedule F)
 - Sale of apple bread, apple cobbler, or apple cider is non-farm income (Schedule C) because the raw product has been processed.

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Note: Honey is an exception. It is reported on schedule F as farm income.

What is a farm?

- Definition of “farmer” varies upon election or credit criteria.
- Generic definition [IRC Section 2032A(e)(4)]
 - The term “farm” includes stock, dairy, poultry, fruit, fur-bearing animal, and truck farms, plantations, ranches, nurseries, ranges, greenhouses or other similar structures used primarily for the raising of agricultural or horticultural commodities, and orchards and woodlands.



Defining a farm

- Examples of other locations in the Internal Revenue Code (IRC) and Treasury Regulations (TR) where this language with minor variation is used to define “farm” are:
- Gross income of farmers [TR Section 1.61-4(d)]
- Soil and water conservation expenses [TR Section 1.175-3]
- Estimated taxes [TR Section 1.6073-1(b)(2)]
- Excise tax on gasoline [IRC Section 6420(c)(2)]
- Meaning of terms; excise tax on gasoline [TR Section 48.6420-4(c)]
- The list above is not all-inclusive, taxpayers and tax preparers can find many other references that define “farm” for tax purposes.

Defining Farmer

- A farmer is an individual who is engaged in farming per the definition found above (IRS Publication 225, page 1, “You are in the business of farming if you cultivate, operate, or manage a farm for profit, either as an owner or tenant”).
- Generally, the farmer has a profit motive when operating a farming business.
 - Hobby Loss Rules - IRS uses nine factors found in IRC Section 183 to determine a business’ profit motive.

Estimated Tax Payments [IRC § 6654(i)(2)]

- For estimated tax purposes, IRS considers a producer a “farmer” if
 - Two-thirds of the producer’s gross income is derived from farming;
 - Single estimated tax payment by the 15th of the month that follows the close of their tax year or
 - Make payment in full of their income tax liability by the first of the third month following the close of their tax year. (Calendar-year taxpayers: 15th of January or 1st of March).



Department of the Treasury
Internal Revenue Service

Example 1 – Colorado Sheep Producer

- Jose raises sheep full-time in the alpine meadows of Colorado.
- Jose sells market lambs and wool shorn from the flock.
- This is Jose’s primary source of income with over two-thirds of his income coming from this activity.
- He has a profit motive relative to his business activities.
- Jose is a farmer for income tax purposes and would qualify for the estimated tax payments provisions.

Example 2 – Herb Farm with off-farm income

- Susie grows herbs for sale at her local farmer's market.
- Susie's main source of income is her work as a computer engineer for a software company. Her herb sales are a small part of her total income.
- Even though she has a horticultural activity, less than 2/3s of her income is from farming. So, she would not qualify for the special benefits for estimated tax payments. If Susie can show she has a profit motive, her herb production would qualify as a farm activity and any income and expenses would be recorded on an IRS Form 1040 Schedule F.

Installment Sale of Farm Products (IRC § 453)

- Cash-basis farmers are permitted to report income from the sale of farm products when income is received.
- They are not required to maintain inventories.
- Sales reported in the year of payment, not production.
- The contract must specify that the farmer can only receive the payment in the subsequent year to production, even if the delivery of the production occurred in the year of production.
- Producer must meet the generic definition of a farmer (slide 11).

Current Year Deduction of Fertilizer and Lime

[IRC § 180]

- Annual election to deduct expenses for fertilizer and lime in the current year
 - even though the fertilizer and lime provide more than one year's economic benefit.
- The farmer, therefore, does not capitalize this expense to match the economic life of this production input.
- Producer must meet the generic definition of a farmer (slide 11).



Business Use of a Farm Vehicle -- a Safe Harbor [Treas. Reg. § 1.274-6T(b)]

- Farmers may deduct up to 75 percent of their farm vehicle expenses as qualified business expenses without the business record substantiation (a log).
- This safe harbor is helpful to beginning farmers and ranchers.
- Producer must meet the generic definition of a farmer (slide 11).

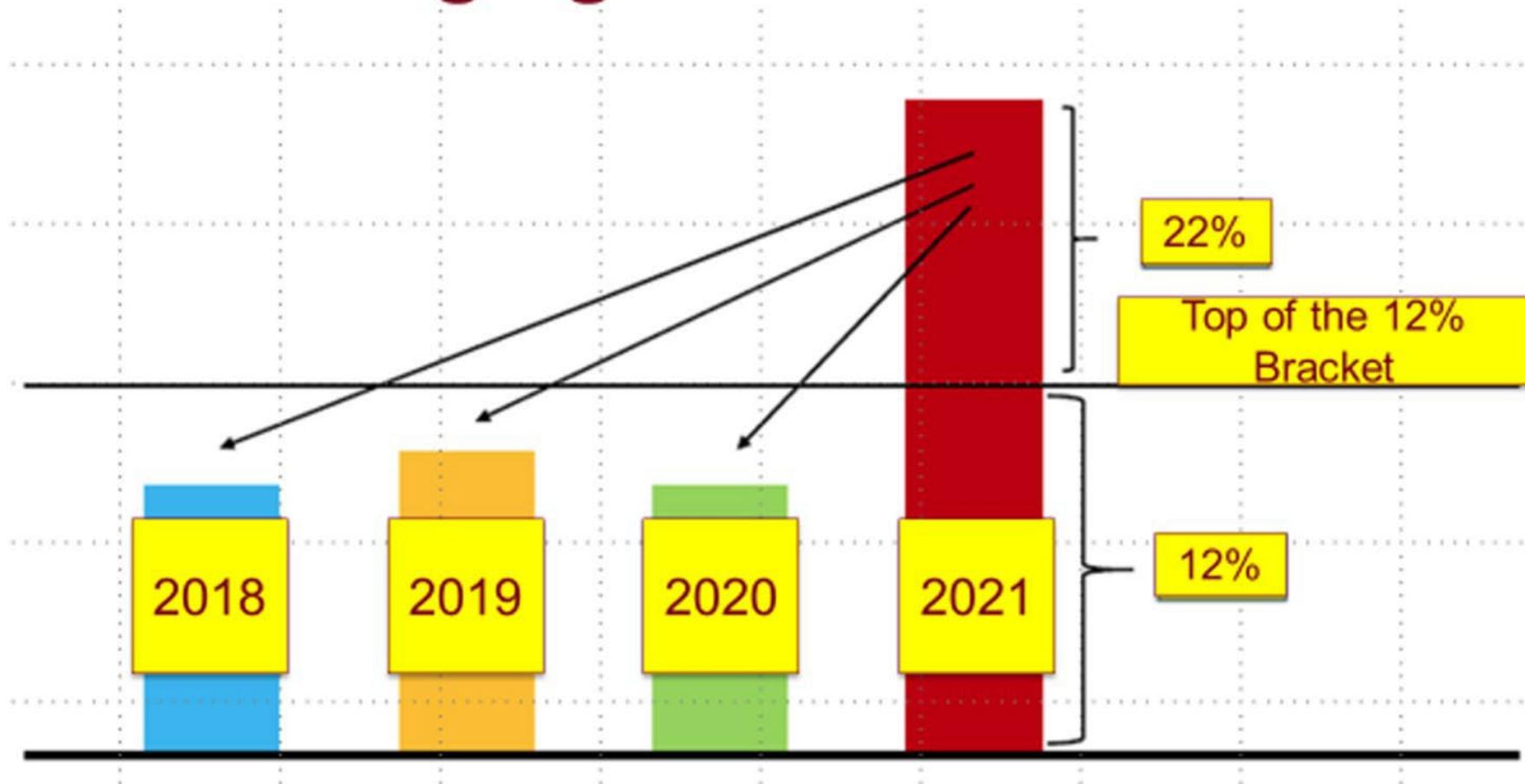


Farm Income Averaging

- Individual taxpayers who qualify as a farmer under IRC Section 1301 may average their farm income.
- This provides for the opportunity to “level” income tax liabilities over a period of years.
- The usefulness of this provision is based upon the individual circumstances of a particular taxpayer’s situation.
- Forestry does not qualify for Income Averaging.
- Producer must meet the generic definition of a farmer (slide 11).



Income Averaging



Questions



New Farmer Tax Topics

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RuralTax.org/newfarmertax

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How to Choose A Tax Preparer

Choosing a tax preparer

1. Check the Preparer's Qualifications.

- CPA, EA, LTP, LTC, CFP, PTIN – many types of qualifications
- [Use the IRS Directory of Federal Tax Return Preparers with Credentials and Select Qualifications.](#)

2. Check the Preparer's History.

- Ask the Better Business Bureau about the preparer.
- Check for disciplinary actions and the license status
 - CPA -- State Board of Accountancy
 - Attorney -- State Bar Association
 - Enrolled Agents -- [verify enrolled agent status](#) page on IRS.gov

Choosing a tax preparer

3. Ask about experience with farm, ranch, forest land returns

- Specialized tax rules
- Prefer they have range of experiences similar to your return

4. Ask about Service Fees.

- Fees often by the hour or by the form
- Ask about charges for phone calls and emails
- Avoid preparers who base fees on a percentage of the refund or who boast bigger refunds than their competition.
- When asking about a preparer's services and fees, don't give them tax documents, Social Security numbers or other information.

Choosing a tax preparer

5. Make Sure the Preparer is Available.

- Taxpayers may want to contact their preparer early summer
- Avoid fly-by-night preparers

6. Ask how they handle “grey” areas

- Best if on same page

7. Find out limits on audit representation

- Not all preparers can represent you or are willing

Tax Season Tips -- Choosing a tax preparer

- **Provide Records and Receipts.** Good preparers will ask to see a taxpayer's records and receipts. They'll ask questions to figure things like the total income, tax deductions and credits.
- **Never Sign a Blank Return.** Don't use a tax preparer who asks a taxpayer to sign a blank tax form.

Tax Season Tips -- Choosing a tax preparer

- **Review Before Signing.**

- Ask questions
- Refund should go directly to taxpayer
- Get a copy of the completed tax return.

- **Ensure the Preparer Signs and Includes Their PTIN.**

- All paid tax preparers must have a Preparer Tax Identification Number.
- By law, paid preparers must sign returns and include their PTIN.

Choosing a tax preparer

- **Report Abusive Tax Preparers to the IRS.**
 - Most tax return preparers are honest and provide great service to their clients.
 - Report abusive tax preparers and suspected tax fraud to the IRS. Use [Form 14157, Complaint: Tax Return Preparer. If a taxpayer suspects a tax preparer](#) filed or changed their return without the taxpayer's consent, they should file [Form 14157-A](#), Return Preparer Fraud or Misconduct Affidavit.

Resource Links

- Rural Tax.org
 - <http://www.ruraltax.org>
 - <http://ruraltax.org/beginningfarmer-tax>
- USDA Farmers Website
 - <https://www.farmers.gov/taxes>
- IRS Publication 225: Farmers Tax Guide
 - <https://www.irs.gov/pub/irs-pdf/p225.pdf>
- Land Grant University Tax Education Foundation
 - <https://taxworkbook.com>



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Questions



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