Taxes and Beginning Farmers  2/2/11

Dennis Kauppila, UVM Extension

Lauren Jarvi, EA, CFP
M. Sciabarrasi, UNH Coop Extension
C.Zintel, Farm Credit East, Bedford, NH

Pub 225
Farmer’s Tax Guide

www.irs.gov

A comprehensive guide to all the subjects related to filing income taxes for farm businesses

Farm Income Tax Basics

- Start-up Decisions
- Hobby or Business
- Business Income & Expenses
- Depreciation
- Sales of Business Property
- Employer-employee Issues
- Self-Employment Tax
Types of Taxes

**Person, not business**
- State, Fed Income
- Property
- Tax on Capital Gain
- Estate

**Businesses only**
- Schedule C or F
- Self Employment
- Employer paperwork
- Sales
- Excise

Start-up Decisions

- Choice of entity
- How to keep financial records
  - System you are comfortable with
  - Can keep up to date
  - Catch all deductible expenses
- Register business name w/Sec’y of State
- Open business checking account

Hobby or business?

- ‘Not-for-profit farming’ FTG p.26
  - For profit, deduct expenses on Sch F
  - Not-for-profit
    - Income on Form 1040 line 21
    - Exp on Sch A, limits on expenses
    - Like all hobbies
- Farming for profit- 9 factors, FTG p 27
What is a Farm?

"Business of farming...cultivate, operate or manage a farm for profit...not timber..."

"A farm includes livestock, dairy, poultry, fish, fruit, and truck farms. ...fish farm...plant nursery..."

"orchards, plantations, ranches...greenhouses...bees..."

FTG p 1, 28, 74, 81, 84

Farm Records and Tax Reports

- Categorized list of incomes, expenses
- List of assets bought, sold, or traded
- 1099 info returns
- Payroll records
- Inventory
- Accounts receivable
Business profits

- Income – Expense = Profit
- Profit moves onto Form 1040, taxed at Fed and State levels
- No tax on business profits (at business level)
  - Sole proprietor
  - Partnership
  - LLC taxed as partnership

Farm Income

Reported on Schedule F (Part I or Part III)
Sales of products raised or grown, sales of farm products purchased for resale, income from farm related services, payments from Agricultural Programs …includes barter (p17) ….

Income from normal business operations
Money received during the year

Farm Expenses

Reported on Schedule F (Part II)

“Ordinary + necessary costs of operating a farm for profit are deductible business exp.”
Car + truck, c. hire, deprec., feed, fert+lime, freight +t, gas fuel oil, ins, int, labor hired, rent/lease, repairs, seeds + plants, supplies, taxes, utilities, vet br med, other expenses

Expenses paid during the year by cash, check, credit card. Biz expenses only, NOT personal
Depreciation

- Using up/wearing out of an asset
- 'Spread' its cost over several years
- Identify it
  - When you bought/sold it
  - What you paid for it/got for it
- Very specific rules about
  - # years to D it and how fast to D it
- # years Actual life not same as D life

Depreciation- add ons

- Section 179 Expense Deduction
  - "Election to recover all or part of the cost of qualifying property by deducting it in the year placed in service."

- 'Listed Property' handled differently
  - Cars, computers, farm pickup
  - Business and personal use
Sale of Business Property

- Usually not a farm product
- Usually on the farm > 1 year
- Could be a gain or a loss
- May be taxed at lower, Capital Gains rate, not Ordinary Income rate, no SE tax
- Records important
  - Date of sale, sales price, if trade is involved

Self-Employment Tax

- Paid by owner of business
  - Based on profit shown on Schedule F or C
  - Owner is usually not an employee
- Schedule SE
- Not subject to SE tax
  - Sale of business property
  - Rent
  - Investment income

Hired Labor

- Wages, taxes, benefits deductible expenses
- Can hire family members
- Taxes, withholding
  - Federal and State, based on W-4
  - Fed, State unemployment tax
  - Fed Soc Security Tax
- Workers Compensation Insurance ($10,000)
- Employer has responsibilities to employees
Employees
- Need Employer ID number, Form SS-4
  - Legal obligations, Form I-9
- Employee, you control
  - What is done and how to do it
  - How worker is paid and if reimburse expenses
  - Have continuing relationship
- Independent Contractor
  - Does same service for others
  - In biz for themselves

Owner’s Labor
- Owner does NOT get paid a wage/salary
- Owner is not an employee
- Owner takes a ‘draw’ not taxable
- Owner gets profit- return to investment and time
- Owner pays tax on profit

Estate Tax
- If you die with lots of assets, your heirs may have to pay an Estate Tax
  - Federal > $5 million
  - VT > $2 million
  - BIG political football
Vermont Taxes

- Homestead Declaration
  - All residents, watch business use of building
- Property Tax
  - Use Value Appraisal of Farm and Forest Land
  - Gross sales > $2,000 or at least 25 A
  - Maps, application due in Montpelier by 9/1
- Sales Tax, not on food
- VT Dept of Taxation, www.state.vt.us/tax

DIY or Professional?

- Been doing your own?
- Comfort level
- Hire someone first few years
- TurboTax not like talking w/your pro
- How to choose
- Ask your friends
- Registered Preparer, EA, CPA

More Questions?

Resources

- www.IRS.gov
- www.ruraltax.org
- Dennis Kauppila – dennis.kauppila@uvm.edu

Thank you!
Introduction

You are in the business of farming if you cultivate, operate, or manage a farm for profit, either as owner or tenant. A farm includes livestock, dairy, poultry, fish, fruit, and truck farms. It also includes plantations, ranches, ranges, and orchards.

This publication explains how the federal tax laws apply to farming. Use this publication as a guide to figure your taxes and complete your farm tax return. If you need more information on a subject, get the specific IRS tax publication covering that subject. We refer to many of these free publications throughout this publication. See chapter 16 for information on ordering these publications.

The explanations and examples in this publication reflect the Internal Revenue Service's interpretation of tax laws enacted by Congress, Treasury regulations, and court decisions. However, the information given does not cover every situation and is not intended to replace the law or change its meaning. This publication covers subjects on which a court may have made a decision more favorable to taxpayers than the interpretation of the Service. Until these differing interpretations are resolved by higher court decisions, or in some other way, this publication will

Acknowledgment: The valuable advice and assistance given us each year by the National Farm Income Tax Extension Committee is gratefully acknowledged.

Get forms and other information faster and easier by:

Internet IRS.gov
**Form 1040**

**U.S. Individual Income Tax Return**

**2010**

**IR-1 Use Only—Do not write or staple in this space.**

**OMB No. 1545-0074**

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### Name, Address, and SSN

- Print clearly
- See separate instructions.

#### Presidential Election Campaign
- Check here if you, or your spouse if filing jointly, want $3 to go to this fund.
- ☐ You  ☐ Spouse

#### Filing Status
1. ☐ Single
2. ☐ Married filing jointly (even if only one had income)
3. ☐ Married filing separately. Enter spouse’s SSN above and full name here.

#### Exemptions

| a | Yourself. If someone can claim you as a dependent, do not check box 6a. |
| b | Spouse |

#### Dependents:

<table>
<thead>
<tr>
<th>(1) First name</th>
<th>Last name</th>
<th>(2) Dependent’s social security number</th>
<th>(3) Dependent’s relationship to you</th>
<th>(4) ☐ if child under age 17 qualifying for child tax credit (see page 15)</th>
</tr>
</thead>
</table>

#### Income

- wages, salaries, tips, etc. Attach Form(s) W-2
- Taxable interest. Attach Schedule B if required
- Tax-exempt interest. Do not include on line 8a.
- Ordinary dividends. Attach Schedule B if required
- Qualified dividends
- Taxable refunds, credits, or offsets of state and local income taxes
- Alimony received
- Business income or (loss). Attach Schedule C or C-EZ
- Capital gain or (loss). Attach Schedule D if required. If not required, check here
- Other gains or (losses). Attach Form 4797
- IRA distributions
- Pensions and annuities
- Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E
- Farm income or (loss). Attach Schedule F
- Unemployment compensation
- Social security benefits
- Other income. List type and amount

#### Adjusted Gross Income

- Educator expenses
- Certain business expenses of reservists, performing artists, and fee-basis government officials. Attach Form 2106 or 2106-EZ
- Health savings account deduction. Attach Form 8889
- Moving expenses. Attach Form 3903
- One-half of self-employment tax. Attach Schedule SE
- Self-employed SEP, SIMPLE, and qualified plans
- Self-employed health insurance deduction
- Penalty on early withdrawal of savings
- Alimony paid
- IRA deduction
- Student loan interest deduction
- Tuition and fees. Attach Form 8917
- Domestic production activities deduction. Attach Form 8903

#### Total Income

- Add lines 7 through 21. This is your total income

#### Subtract line 36 from line 22. This is your adjusted gross income
### Tax and Credits
- **Amount from line 37 (adjusted gross income)**: 38
- **Check**
  - [ ] You were born before January 2, 1946
  - [ ] Blind
- **Total boxes checked**: 39a
- **If**
  - [ ] Spouse was born before January 2, 1946
  - [ ] Blind
- **Exemptions**
  - Multiply $3,650 by the number on line 6d
- **Taxable income**: Subtract line 42 from line 41. If line 42 is more than line 41, enter -0-
- **Tax**
  - (see instructions)
- **Alternative minimum tax**
  - (see instructions)
- **Add lines 44 and 45**
- **Foreign tax credit**
  - Attach Form 1116 if required
- **Credit for child and dependent care expenses**
  - Attach Form 2441
- **Education credits** from Form 8863
- **Retirement savings contributions credit**
  - Attach Form 8880
- **Child tax credit**
  - (see instructions)
- **Residential energy credits**
  - Attach Form 5695
- **Other credits from Form**
  - a [ ] 3800
  - b [ ] 8903
  - [ ] 8810
  - [ ] 8862
- **Add lines 47 through 53. These are your total credits**
- **Subtract line 54 from line 46. If line 54 is more than line 46, enter -0-**

### Other Taxes
- **Self-employment tax**
  - Attach Schedule SE
- **Unfiled social security and Medicare tax**
  - from Form: a [ ] 4137
  - b [ ] 8919
- **Additional tax on IRAs, other qualified retirement plans, etc.**
  - Attach Form 5329 if required
- **Earned income credit (EIC)**
- **Nontaxable combat pay election**
- **Additional child tax credit**
  - Attach Form 8812
- **American opportunity credit**
  - from Form 8863
- **First-time homebuyer credit**
  - from Form 5405
- **Amount paid with request for extension to file**
- **Excess social security and tier 1 RRTA tax withheld**
- **Credit for federal tax on fuels**
  - Attach Form 4136
- **Add lines 61 through 67. These are your total tax payments**

### Payments
- **Federal income tax withheld from Forms W-2 and 1099**
- **2010 estimated tax payments and amount applied from 2009 return**
- **Making work pay credit**
  - Attach Schedule M
- **Earned income credit (EIC)**
  - b Nontaxable combat pay election
  - d Account number
- **Add lines 61 through 71. These are your total payments**

### Refund
- **If line 72 is more than line 60, subtract line 60 from line 72. This is the amount you overpaid**
- **Amount of line 73 you want refunded to you**
  - If Form 8888 is attached, check here
- **Direct deposit?**
  - b Routing number
  - c Type: Checking
  - [ ] Savings
- **Amount of line 73 you want applied to your 2011 estimated tax**

### Amount You Owe
- **Amount you owe**
  - Subtract line 72 from line 60.
  - For details on how to pay, see instructions
  - **Estimated tax penalty**

### Third Party Designee
- **Do you want to allow another person to discuss this return with the IRS?**
  - [ ] Yes. Complete below.
  - [ ] No

### Sign Here
- **Your signature**
- **Date**
- **Your occupation**
- **Daytime phone number**
- **Spouse's signature. If a joint return, both must sign.**
- **Date**
- **Spouse's occupation**

### Paid Preparer
- **Print/Type preparer's name**
- **Preparer's signature**
- **Date**
- **Check**
  - [ ] If self-employed
- **PTIN**
- **Firm's name**
- **Firm's EIN**
- **Phone no.**

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Form 1040 (2010)
### Part I: Farm Income—Cash Method
Complete Parts I and II (Accrual method. Complete Parts I and III, and Part I, line 11.) Do not include sales of livestock held for draft, breeding, sport, or dairy purposes. Report these sales on Form 4797.

<table>
<thead>
<tr>
<th>Line</th>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Sales of livestock and other items you bought for resale</td>
<td>1</td>
</tr>
<tr>
<td>2</td>
<td>Cost or other basis of livestock and other items reported on line 1</td>
<td>2</td>
</tr>
<tr>
<td>3</td>
<td>Subtract line 2 from line 1</td>
<td>3</td>
</tr>
<tr>
<td>4</td>
<td>Sales of livestock, produce, grains, and other products you raised</td>
<td>4</td>
</tr>
<tr>
<td>5a</td>
<td>Cooperatives distributions (Form(s) 1099-PATR) 5b Taxable amount</td>
<td>5b</td>
</tr>
<tr>
<td>6a</td>
<td>Agricultural program payments (see instructions)</td>
<td>6a</td>
</tr>
<tr>
<td>7</td>
<td>Commodity Credit Corporation (CCC) loans (see instructions):</td>
<td></td>
</tr>
<tr>
<td>a</td>
<td>CCC loans reported under election</td>
<td>7a</td>
</tr>
<tr>
<td>b</td>
<td>CCC loans forfeited</td>
<td>7b</td>
</tr>
<tr>
<td>c</td>
<td>If election to defer to 2011 is attached, check here</td>
<td>8d</td>
</tr>
<tr>
<td>8</td>
<td>Crop insurance proceeds and federal crop disaster payments (see instructions)</td>
<td>7c</td>
</tr>
<tr>
<td>a</td>
<td>Amount received in 2010 8b Taxable amount</td>
<td>8b</td>
</tr>
<tr>
<td>b</td>
<td>CUSTOM HIRING (MACHINE WORK) INCOME</td>
<td>9</td>
</tr>
<tr>
<td>10</td>
<td>Other income, including federal and state gasoline or fuel tax credit or refund</td>
<td>10</td>
</tr>
<tr>
<td>11</td>
<td>Gross income. Add amounts in the right column for lines 3 through 10. If you use the accrual method to figure your income, enter the amount from Part III, line 51</td>
<td>11</td>
</tr>
</tbody>
</table>

### Part II: Farm Expenses—Cash and Accrual Method
Do not include personal or living expenses such as taxes, insurance, or repairs on your home.

<table>
<thead>
<tr>
<th>Line</th>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>12</td>
<td>Car and truck expenses (see instructions). Also attach Form 4562</td>
<td>12</td>
</tr>
<tr>
<td>13</td>
<td>Chemicals</td>
<td>13</td>
</tr>
<tr>
<td>14</td>
<td>Conservation expenses (see instructions)</td>
<td>14</td>
</tr>
<tr>
<td>15</td>
<td>Custom hire (machine work)</td>
<td>15</td>
</tr>
<tr>
<td>16</td>
<td>Depreciation and section 179 expense deduction not claimed elsewhere (see instructions)</td>
<td>16</td>
</tr>
<tr>
<td>17</td>
<td>Employee benefit programs other than on line 25</td>
<td>17</td>
</tr>
<tr>
<td>18</td>
<td>Feed</td>
<td>18</td>
</tr>
<tr>
<td>19</td>
<td>Fertilizers and lime</td>
<td>19</td>
</tr>
<tr>
<td>20</td>
<td>Freight and trucking</td>
<td>20</td>
</tr>
<tr>
<td>21</td>
<td>Gasoline, fuel, and oil</td>
<td>21</td>
</tr>
<tr>
<td>22</td>
<td>Insurance (other than health)</td>
<td>22</td>
</tr>
<tr>
<td>23</td>
<td>Interest:</td>
<td></td>
</tr>
<tr>
<td>a</td>
<td>Mortgage (paid to banks, etc.)</td>
<td>23a</td>
</tr>
<tr>
<td>b</td>
<td>Other</td>
<td>23b</td>
</tr>
<tr>
<td>24</td>
<td>Labor hired (less employment credits)</td>
<td>24</td>
</tr>
<tr>
<td>25</td>
<td>Pension and profit-sharing plans</td>
<td>25</td>
</tr>
<tr>
<td>26</td>
<td>Rent or lease (see instructions):</td>
<td>26</td>
</tr>
<tr>
<td>a</td>
<td>Vehicles, machinery, and equipment</td>
<td>26a</td>
</tr>
<tr>
<td>b</td>
<td>Other (land, animals, etc.)</td>
<td>26b</td>
</tr>
<tr>
<td>27</td>
<td>Repairs and maintenance</td>
<td>27</td>
</tr>
<tr>
<td>28</td>
<td>Seeds and plants</td>
<td>28</td>
</tr>
<tr>
<td>29</td>
<td>Storage and warehousing</td>
<td>29</td>
</tr>
<tr>
<td>30</td>
<td>Supplies</td>
<td>30</td>
</tr>
<tr>
<td>31</td>
<td>Taxes</td>
<td>31</td>
</tr>
<tr>
<td>32</td>
<td>Utilities</td>
<td>32</td>
</tr>
<tr>
<td>33</td>
<td>Veterinary, breeding, and medicine</td>
<td>33</td>
</tr>
<tr>
<td>34</td>
<td>Other expenses (specify):</td>
<td>34</td>
</tr>
<tr>
<td>a</td>
<td></td>
<td>34a</td>
</tr>
<tr>
<td>b</td>
<td></td>
<td>34b</td>
</tr>
<tr>
<td>c</td>
<td></td>
<td>34c</td>
</tr>
<tr>
<td>d</td>
<td></td>
<td>34d</td>
</tr>
<tr>
<td>e</td>
<td></td>
<td>34e</td>
</tr>
<tr>
<td>f</td>
<td></td>
<td>34f</td>
</tr>
</tbody>
</table>

### Total Expenses
Add lines 12 through 34f. If line 34f is negative, see instructions.

### Net Farm Profit or Loss
Subtract line 35 from line 11. Partnerships, see instructions.

* If a profit, enter the profit on both Form 1040, line 15, and Schedule SE, line 1a; on Form 1040-NR, line 19; or on Form 1041, line 6.
* If a loss, you must go to line 37.

If you have a loss, you must check the box that describes your investment in this activity and whether you received any applicable subsidy (see instructions).

* If you checked 37a, enter the loss on both Form 1040, line 18, and Schedule SE, line 1a; on Form 1040-NR, line 19; or on Form 1041, line 6.
* If you checked 37b, your loss may be limited. See instructions.
### Part III  Farm Income—Accrual Method (see instructions)

Do not include sales of livestock held for draft, breeding, sport, or dairy purposes. Report these sales on Form 4797 and do not include this livestock on line 46 below.

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>38</td>
<td>Sales of livestock, produce, grains, and other products</td>
</tr>
<tr>
<td>39a</td>
<td>Cooperative distributions (Form(s) 1099-PATR)</td>
</tr>
<tr>
<td>39b</td>
<td>Taxable amount</td>
</tr>
<tr>
<td>40a</td>
<td>Agricultural program payments</td>
</tr>
<tr>
<td>40b</td>
<td>Taxable amount</td>
</tr>
<tr>
<td>41</td>
<td>Commodity Credit Corporation (CCC) loans:</td>
</tr>
<tr>
<td>41a</td>
<td>CCC loans reported under election</td>
</tr>
<tr>
<td>41b</td>
<td>CCC loans forfeited</td>
</tr>
<tr>
<td>41c</td>
<td>Taxable amount</td>
</tr>
<tr>
<td>42</td>
<td>Crop insurance proceeds</td>
</tr>
<tr>
<td>43</td>
<td>Custom hire (machine work) income</td>
</tr>
<tr>
<td>44</td>
<td>Other income, including federal and state gasoline or fuel tax credit or refund</td>
</tr>
<tr>
<td>45</td>
<td>Add amounts in the right column for lines 38 through 44</td>
</tr>
<tr>
<td>46</td>
<td>Inventory of livestock, produce, grains, and other products at beginning of the year</td>
</tr>
<tr>
<td>47</td>
<td>Cost of livestock, produce, grains, and other products purchased during the year</td>
</tr>
<tr>
<td>48</td>
<td>Add lines 46 and 47</td>
</tr>
<tr>
<td>49</td>
<td>Inventory of livestock, produce, grains, and other products at end of year</td>
</tr>
<tr>
<td>50</td>
<td>Cost of livestock, produce, grains, and other products sold. Subtract line 49 from line 48*</td>
</tr>
</tbody>
</table>

*If you use the unit-livestock-price method or the farm-price method of valuing inventory and the amount on line 48 is larger than the amount on line 48, subtract line 48 from line 49. Enter the result on line 50. Add lines 45 and 50. Enter the total on line 51 and on Part I, line 11.

### Part IV  Principal Agricultural Activity Codes

**CAUTION**

File Schedule C (Form 1040) or Schedule C-EZ (Form 1040) instead of Schedule F if (a) your principal source of income is from providing agricultural services such as soil preparation, veterinary, farm labor, horticultural, or management for a fee or on a contract basis, or (b) you are engaged in the business of breeding, raising, and caring for dogs, cats, or other pet animals.

These codes for the Principal Agricultural Activity classify farms by their primary activity to facilitate the administration of the Internal Revenue Code. These six-digit codes are based on the North American Industry Classification System (NAICS).

Select the code that best identifies your primary farming activity and enter the six digit number on page 1, line B.

#### Crop Production

- 11100  Oilsand and grain farming
- 111210  Vegetable and melon farming

- 111300  Fruit and tree nut farming
- 111400  Greenhouse, nursery, and floriculture production
- 111900  Other crop farming

#### Animal Production

- 112111  Beef cattle ranching and farming
- 112112  Cattle feedlots
- 112120  Dairy cattle and milk production
- 112210  Hog and pig farming
- 112300  Poultry and egg production
- 112400  Sheep and goat farming
- 112510  Aquaculture
- 112900  Other animal production

#### Forestry and Logging

- 113000  Forestry and logging (including forest nurseries and timber tracts)
Welcome to the Rural Tax Education website. This website provides farmers and ranchers, other agricultural producers and Extension educators with a source for agriculturally related income and self-employment tax information that is both current and easy to understand.

Tax issues are important for agricultural operations because income and self-employment taxes are a major cost and also because more and more USDA programs are being linked to a producer’s federal income tax return.

Hot Topic

The Tax Relief Act of 2010 changes depreciation and Section 179 expensing options for recent years and options available for 2011 and 2012.

Click here to read

Webinars

As in Uncertain Times
Learn about key changes in the new Tax Law and how they affect agricultural producers.

February 7, 12:00 Noon ET.

Click here for more details.

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