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Tax Considerations for Agritourism Operations*

***Kevin Burkett**, Extension Associate*
Clemson University

***Rob Holcomb**, Extension Educator*
University of Minnesota

Introduction

Farms may often look for opportunities to generate additional revenue for their operation. One such activity that has continued to gain popularity is agritourism. Perhaps that term is already familiar; it includes activities such as farm stays, you-pick operations, farm-to-table events, educational classes or tours, and various entertainment activities, such as corn mazes. These activities are generally occurring on-farm, so it is often assumed that they are reported the same as agricultural production. However, as they are not true farm production, per se, they are treated differently. There are tax, legal, and operational considerations for farming versus agritourism activities.

Farming vs. Agritourism Activities

To briefly recap what is considered a farm for tax purposes, it includes livestock, dairy, poultry, fish, fruit, and truck farms including plantations, ranches, ranges, orchards, and groves. It involves cultivation, operation, or management of a farm for profit, either as an owner or tenant. (For further discussion on this topic, see *Farm, Farming, and Who's a Farmer for Tax Purposes* on RuralTax.org).

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True farm income is reported on *Schedule F (Form 1040), Profit or Loss From Farming* and includes cultivation and sale of farm crops, crop insurance proceeds, agricultural program payments, patronage dividends, incidental custom or processing activities, and sale of crop shares (if you materially participate). It does not include activities such as only buying and reselling agricultural products, or processing of a raw agricultural product beyond its unmanufactured state (which would be deemed processing).

Example 1:

Theresa grows many vegetables on her farm including tomatoes, onions, peppers, and herbs. Theresa does not want any of her produce to go to waste. When she has leftover produce, she offers to host a canning class at her farm to teach people how to make and can salsa. She sells tickets to the canning class. The participants get to keep one jar of salsa, and she sells the remaining jars at her farm stand. The ticket to Theresa's class is an agritourism activity and the salsa is a value-added product.

This can sometimes become confusing for operators because, oftentimes, these activities may occur simultaneously, so the activities are inadvertently recorded and reported together. There are certain tax provisions that are only available for farming operations and so, for that reason, it is important to separate the activities via recordkeeping of the farm. One example is *Schedule J (Form 1040), Income Averaging for Individuals with Income From Farming or Fishing*, which is only available to commercial farming activities.

Aside from tax considerations, there are other reasons to separate out this information. When meeting with lenders, insurance companies, or signing up for USDA programs, the agent would want a true accounting of each activity. If a loan, insurance policy, or government program is strictly for crop production, it becomes important to be able to make that distinction. Incidental processing or agritourism activities can be reported on *Schedule F (Form 1040), Profit or Loss From Farming*, but when they start to become bona fide activities, they would need to be reported on *Schedule C (Form 1040), Profit or Loss from Business (Sole Proprietorship)*.

Schedule C (Form 1040), Profit or Loss from Business (Sole Proprietorship) captures all other small business activities. Selling entrance tickets, hot food items, tours, dinners, value-added products, or crafts are considered other small business sales. Normally, a producer would want to have a separate business bank account to be able to separate the farm business versus personal accounts; if they become involved in *Schedule C (Form 1040), Profit or Loss from Business (Sole Proprietorship)* activities, it is then advisable to have a third account to separate farm business versus agritourism.

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Example 2:

In the fall the Appleseed family hosts a fall festival. Customers come out to the farm to enjoy you-pick apples, tractor rides, cider and donuts, and face painting. While there are numerous activities occurring, only the apples are related to the true production of the farm. The sales of apples would be recorded line 2 of *Schedule F (Form 1040), Profit or Loss From Farming*. They may be using the apples as an ingredient in the cider or donuts, which would be reported as an intra-business sale from the farm *Schedule F (Form 1040), Profit or Loss From Farming* to the *Schedule C (Form 1040), Profit or Loss from Business (Sole Proprietorship)* business. However, when the cider or donuts are sold to customers it is on line 1 of *Schedule C (Form 1040), Profit or Loss from Business (Sole Proprietorship)*. Each activity should record the correct revenues and expenses associated with it.

Tax Management

For tax management, the income from both farming and agritourism activities becomes summarized through the tax return. *Schedule F (Form 1040), Profit or Loss From Farming* for farming and *Schedule C (Form 1040), Profit or Loss from Business (Sole Proprietorship)* for all other small business sales. The resulting calculation from these forms ends up going to *Schedule 1 (Form 1040), Additional Income and Adjustments to Income* (line 3 and line 6) of the *Form 1040, U. S. Individual Income Tax Return*. These activities, along with other sources of income for the taxpayer(s), make up the total income reported on the return. Other sources could be wages or *Form W-2, Wage and Tax Statement* income, investments, rentals, other small businesses, or spousal income. It is prudent to understand the main contributors of income for the return to make decisions from a tax management standpoint. Farming or agritourism could make up a large chunk of these activities or only a smaller percentage, depending on the size of the operation in relation to the other activities a taxpayer may have. Both *Schedule F (Form 1040), Profit or Loss From Farming* and *Schedule C (Form 1040), Profit or Loss from Business (Sole Proprietorship)* activities are reportable as self-employment income. Earnings from self-employment are calculated and summarized on *Schedule SE (Form 1040), Self-Employment Tax.* It is important to note that in the case of spouses, it is advisable for each spouse to report earnings from self-employment to earn credits for the social security benefits they may be eligible for later.

Other Considerations

While the focus of this article is on federal tax impacts of agritourism activities, at times, producers may have questions regarding business licenses or state and local taxes for agritourism activities. As a very general rule, states treat agritourism activities differently than farm production activities. Separate business licenses may be required for agritourism. Generally, states will exempt raw farm

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products (and even some farm inputs) from sales tax, while often value-added products, admission tickets, hot foods, or farm stays can be subject to one or more types of sales tax. It is advisable to check with your local authorities, such as state departments of revenue, counties, municipalities, or towns where the activities will be ongoing. As mentioned previously, records of what pertains to the true farm business versus agritourism will be important to correctly report the results from each.

IRS Publications

To access IRS forms, schedules, and publications, go to www.irs.gov and type the publication, form or schedule number or title in the search box.

The following may be of particular interest:

- **IRS Publication 225, Farmer's Tax Guide**: This publication explains how the federal tax laws apply to farming.
- **IRS Publication 583, Starting a Business and Keeping Records**: This publication provides basic federal tax information for people who are starting a business. It also provides information on keeping records and illustrates a recordkeeping system.
- **IRS Schedule F (Form 1040), Profit or Loss From Farming**: This form is used to report farm income and expenses.
- **IRS Schedule C (Form 1040), Profit or Loss from Business (Sole Proprietorship)**: This form is used to report income or loss from a business you operated or a profession you practiced as a sole proprietor.

Additional Topics

This fact sheet was written as part of Rural Tax Education, a national effort including Cooperative Extension programs at participating land-grant universities to provide income tax education materials to farmers, ranchers, and other agricultural producers. For a list of universities involved, other fact sheets and additional information related to agricultural income tax please see RuralTax.org.

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