

## Employment of Family Members\*

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### Introduction

The use of family labor in the farm or ranch operation can pose a number of challenges for farm managers as they try to sort through the vast quantity of regulations. While the day-to-day human-relations components of managing family members in the farm/ranch operation will differ substantially from that of non-family labor, the focus of this fact sheet will address the income tax and regulatory aspects of employing family members.

Generally, the wages that you pay to family members who are also your employees are subject to social security (FICA) and Medicare taxes, federal income tax withholding, and under certain circumstances, federal and state unemployment (FUTA/SUTA).<sup>1</sup> Certain exemptions may apply for your child, spouse, or parent.<sup>2</sup> In addition, employers who pay less than \$150 to one individual per year, or employers who pay less than \$2,500 to all employees in one year may be exempt but there are exceptions to this rule. It is important that you understand these exceptions as noted in IRS publication 51.

### Becoming an Employer

If you have hired labor, you are required to issue a W-2 to each employee, withhold payroll taxes, and deposit payroll taxes in a timely manner. While qualifying family members may be excluded from certain payroll taxes, all employees (family and non-family) must be issued a W-2. To perform any of the aforementioned tasks, the employer must have an employer identification number (EIN). An EIN may be acquired by completing the online application for an employer identification number.

The application for an employer identification number is located in the tools section of the IRS homepage ([www.irs.gov](http://www.irs.gov)).

In some jurisdictions you may be required to register the farm business with your state Department of Revenue.

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<sup>1</sup> Internal Revenue Service. Publication 51. Agricultural Employer's Tax Guide. 2017. [www.irs.gov/pub/irs-pdf/p51.pdf](http://www.irs.gov/pub/irs-pdf/p51.pdf) p. 10.

<sup>2</sup> Ibid. p. 22.

## State vs. Federal Regulations

One major issue of confusion with respect to labor laws are the inconsistencies that exist between State and Federal authorities. In many locations, state and federal regulations are de-coupled. In general, if your state regulations differ from federal regulations, the employer needs to apply the law(s) that offer the most benefit to the employee. Federal labor law will refer to this practice as, “implementing the most protective standard.” Check with both agencies to clarify which rules are “in force.”

## Children and Child Labor Laws

With respect to minor dependent children working in the farming operation, the current United States Department of Labor regulations provide for parental exemptions from most child labor laws. When employing children other than your own, you should consult the current child labor regulations issued by the United States Department of Labor and the Department of Labor for the State where you reside. It is not uncommon for differences to exist when comparing state and federal regulations. It is the responsibility of the employer to check both the Federal and State child labor laws to insure compliance with both agencies.

## FICA/Medicare/FUTA/SUTA

Children under age 18 working for parent-owned unincorporated businesses are exempt from FICA and Medicare. Children under age 21 working for parent-owned unincorporated businesses are exempt from FUTA.<sup>3</sup> Children under age 18 working for a partnership are exempt from FICA and Medicare withholding providing that all partners are parents of the employed children.<sup>4</sup>

A parent employed by a child or a spouse employed by a spouse is exempt from FUTA but still subject to FICA and Medicare withholding.<sup>5</sup>

A dependent child working in the farm business must be a bona-fide employee of the parent-owned business. This means that child must actually perform legitimate services as an employee of the business, the child must be compensated for those services, and the compensation must be reasonable in relation to the services performed.<sup>6</sup> The above rules do not apply to siblings and other relatives. You have the same payroll tax obligations for these family members as you have for employees who are not related to you.

## Documentation (I-9 and W-4)

All new employees, including family members, must complete and sign an I-9 (Employment Eligibility Verification) form. Form I-9 must be completed within three days of hiring.

Employees (including family members) must also complete a form W-4. The form W-4 is used to communicate to the employer how much Federal and/or State income tax to withhold from the employees paycheck. In some cases, individuals may need to fill out a W-4 more than once as their individual situation changes (single – married – married with dependents, age). It is important to encourage family members to keep track of this and the amount of taxes withheld from the paycheck each year.

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<sup>3</sup> The Tax Book. Web Library Edition. 2017. Tax Materials, Inc. p. 5-19.

<sup>4</sup> Ibid. p. 5-19

<sup>5</sup> Ibid. p. 5-19

<sup>6</sup> The Tax Book. Web Library Edition. 2017. Tax Materials, Inc. p. 5-19.

Family members are not exempt from the requirement to complete both form I-9 and W-4. While these forms are not required to be filed with the IRS, they must be made available to applicable state and/or federal agencies upon request.

## Workers' Compensation

Workers' Compensation statutes are intended to provide wage replacement and compensation for employees who suffer work-related injuries or illnesses. Every state has a workers' compensation system under which employer participation is mandatory (participation is not mandatory in Texas). Although each state determines specific aspects of its workers' compensation system, such as employee eligibility requirements and payment schedules, the basic program features are similar from state to state.

Regarding participation, agricultural employers have different requirements from that of non-farm employers. Additionally, farms have the option of whether or not they choose to cover family members who work on the farm or serve as corporate officers in a family farm corporation.

## IRS Publications

To access IRS Publications go to [www.irs.gov](http://www.irs.gov) and click on "Forms and Publications". Then click the "Publication number" under "Download forms and publications by:" Type the publication number in the find box to search for the publication. Publications may be viewed online or downloaded by double clicking on the publication.

- **IRS Publication 225, Farmer's Tax Guide.** Chapter 4 discusses labor hired. Chapter 13 discusses family employees.
- **IRS Publication 51, Agricultural Employers Tax Guide.** Section 12 discusses the employment of family members and associated exemptions from payroll taxes.

## 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](http://RuralTax.org).

Additionally, many states and universities have a guide or checklist for starting a business. These guides often include both state and federal guidelines. Check with your individual state department of revenue, with your University Extension Service, as well as with the IRS.

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This information is intended for educational purposes only. You are encouraged to seek the advice of your tax or legal advisor, or other authoritative sources, regarding the application of these general tax principles to your individual circumstances. Pursuant to Treasury Department (IRS) Circular 230 Regulations, any federal tax advice contained here is not intended or written to be used, and may not be used, for the purpose of avoiding tax-related penalties or promoting, marketing or recommending to another party any tax-related matters addressed herein.

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