

Introduction to Agricultural Federal Tax Issues*

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Introduction

Essentially all farmers, ranchers and other agricultural producers must file a federal tax return and pay federal income and/or self-employment taxes on their net profit. [Farm, Farming and Who's a Farmer for Tax Purposes](#) provides information about IRS definitions of a farm and farmer filing income tax returns. There are special rules on filing dates for those producers that qualify as a farmer (i.e., one who receives more than two-thirds of his or her net income from farming). [Filing Dates and Estimated Tax Payments](#) provides more details regarding qualifications and estimated tax payments.

Income

Each producer needs to file a *Form 1040 U.S. Individual Income Tax Return* (Form 1040). Agricultural producers may have income from their farming business included on multiple attachments to their 1040 return. The Income section on page one of Form 1040 has lines for reporting wages and salaries and many other sources of income. For other income sources, a specific form or schedule that includes both revenue and expenses will need to be filed. *Schedule F: Profit or Loss from Farming* includes all of the income and expenses from operating the farm or ranch. Any net income or loss is included in the income section of the Form 1040 line 18. Forms and schedules that relate to a farm, ranch or other agricultural operation are discussed below.

- **Schedule F.** This schedule is used to calculate the net income from the farming operation. Part I of the schedule has lines to report the various sources of income or revenue. Part II of Schedule F is used to record expenses using agriculturally appropriate categories, for example: fuel, seed, repairs, etc. Depreciation is an expense that requires its own form for income tax purposes. In general, a producer cannot include in expenses the cost of purchasing assets that will be used over time. Instead the cost of the asset is spread out over multiple years and a [depreciation](#) expense allows a portion of the cost to be

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deducted each year. The depreciation topic is separated into multiple parts. See RuralTax.org for a list of the depreciation topics.

- **Form 4797 (Sale of Business Property).** When business assets, such as equipment, are sold, any gain from the sale has special tax treatment. See [Sale of Business Property](#) for more information. The [involuntary conversion](#) of farm assets is also reported on Form 4797. Sometimes business assets are exchanged rather than sold. [Like-kind Exchange \(Trade\) of Business Assets](#) provides more information about trades.
- When livestock are sold due to acts of God, like weather, there are special rules that allow the livestock to be replaced and the sale proceeds do not need to be included on the return. However, the proceeds must be used to replace the livestock within a designated period. See [Weather Related Sales of Livestock](#) for more information.
- **Form 1099s** are informational returns only and are not filed by the individual with his or her Form 1040. The IRS uses the forms to match income reported on the forms with the income the taxpayer reports on his or her tax return. Producers may receive Form 1099s and may also be required to issue them. For a more complete discussion, see [Form 1099 Informational Returns](#).
 - In general a Form 1099-MISC must be issued to any unincorporated business from whom they have purchased more than \$600 worth of services.
 - Producers receiving a Form 1099 will normally report the amount in the income section of Schedule F.
 - Producers will receive Form 1099's for agricultural program payments and for cooperative distributions. Some of the reported payments and distributions may not be taxable. However, they must be reported on the non-taxable income lines included on the Schedule F.

Losses

There are several considerations if losses occur. Losses can be used to offset income from other sources to reduce the income tax obligation in the year of the loss. The losses can also be carried back to reduce taxes in prior years and/or carried forward. [Choices for Your Farm Operating Loss](#) discusses these options. There are also rules if the producer is not "[actively participating](#)" in the business. If the producer is not actively participating, losses may be passive losses and

cannot be used to offset other income. Another consideration is whether the producer is "at risk". The at-risk amount is the amount of the producer's investment in the business. Deductible losses are limited by the amount "at risk". [How Do the At-Risk Rules Apply to a Farm Business](#) discusses the at-risk issues.

If a farm has losses over an extended period, the IRS may classify this operation as a hobby activity rather than a business. [Farm Losses vs. Hobby Losses](#) discusses the tests on which the IRS bases their determination. The document also discusses the records that can be used to prove it is a business.

Self-Employment Tax

Employers withhold FICA and Medicare from their employee's wages or salary. They then match the withheld amount and send it to the IRS. A producer however, pays the full amount as self-employment tax. This is their contribution to social security and Medicare. Unlike income tax which allows a deduction for either the standard deduction or the itemized deductions in calculating taxable income, self-employment tax is paid on all net income earned from the business. The total rate is 15.3%. Because this is paid on all the earnings, it can often be a larger expense than federal income taxes. [Self-Employment Tax](#) discusses this issue in more detail.

IRS Publications

To access Form 1040 or other publications referenced in this paper, go to www.irs.gov and click on “Forms and Publications.” Then click on “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 desired publication.

- **IRS Publication 225, Farmer’s Tax Guide.** This publication covers a wide variety of farm related income tax issues.

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. All of the fact sheets referred to in this document are listed under Fact Sheets.

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