Chapter 2 *
OVERVIEW OF TAXES

Introduction

Farmers, as well as other taxpayers, pay a wide variety of taxes to federal, state and local governments. This chapter provides a brief overview of those taxes to help you understand the context of the tax planning discussed in the chapters that follow.

Property Taxes

Property taxes are imposed on the value of the property you own. The most common property tax is the real property tax imposed by local governments. This tax is generally the principal source of revenue for local governments. Some jurisdictions also impose a property tax on the value of certain personal property, such as motor vehicles licensed for use on public roads and equipment used in a business.

In most jurisdictions, property tax is computed annually by multiplying the assessed value of the property by that year's tax rate. The local government sends a tax bill to each property owner that details how the tax is calculated and when the payment or payments are due.

A failure to pay property taxes results in a tax lien on the property. The lien allows the local government to foreclose on the property, sell it at a public auction, and apply the sales proceeds to the unpaid taxes.

Local governments typically set the tax rate by dividing their approved budgets by the total assessed value of the real property subject to the tax. Therefore, the tax you pay depends on the assessed values of your property relative to the assessed values of all the other property in the local government's jurisdiction. If the assessed value of all property in a jurisdiction increases by 10% but the government's budget does not change, the amount of tax due on each property stays the same because the tax rate decreases by the same 10%.

In some states, land used for farming purposes is assessed at its use value rather than at its fair market value. The use value reflects the value of the property to a farming business rather than the amount a buyer would pay for it for an alternative use, such as recreation or development. The formula for computing the use value of farmland is typically based on commodity prices, farmland rental rates, or other measures of

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the ability of the land to produce income in a farming business. The threshold requirements for use valuation vary by state, but they generally involve evidence of agricultural use, such as planting crops or grazing livestock.

Planning Pointer

Satisfy Use-Value Requirements

In some cases, a small change in your use of land may make it eligible for use valuation and a reduction in property taxes. Changes that cost you less than the taxes you save increase your after-tax income.

Sales Taxes

Most state governments and many local governments impose a sales tax on purchases of goods and some services. The sales tax is collected at the point of purchase by the vendor, who then remits the taxes to the government.

A number of goods are exempt from sales taxes for a variety of reasons. The most common exemption is food purchased in grocery store. Goods purchased as an input for manufacturing are exempt because sales tax will be collected when the final product is sold. Most states have a sales tax exemption list of farm inputs, such as equipment, seeds, feed, fertilizer, lubricants, animal bedding, and livestock drugs. To qualify for a sales tax exemption that is based on the buyer's use of the good, the buyer generally must provide the seller an exemption certificate or other evidence that the purchase is sales tax-exempt.

In most states, farmers who regularly sell goods that are subject to sales tax may be required to obtain a seller's permit, an identification number and, in some states or municipalities, a business license, and they must collect the sales tax at the point of sale. The collected sales taxes must be remitted to the government periodically with a tax return that reports the taxable sales.

Sellers are not required to collect sales tax on goods shipped to out-of-state buyers if the seller does not have a sufficient physical presence in the buyer's state to be treated as doing business in that state.

Use Taxes

Purchases that would be subject to a state or local sales tax if the seller had a physical presence in the buyer's state are subject to an equivalent tax called the use tax. Buyers are responsible for self-reporting and paying use tax, generally when they file their state income tax returns. Unlike sales tax, use tax is not collected at the point of sale, and unlike property tax, the government does not send a use-tax bill.

Example 2.1: Use Tax

Seth Shapiro bought a computer from an out-of-state seller that had no retail location in Seth's state. The seller was not required to collect—and did not collect—sales tax on Seth's purchase. If Seth purchased the computer from a seller in his own state, the seller would collect a 6% sales tax from Seth and remit it to the state government. Seth must report the purchase to his state government and pay a 6% use tax.

Excise Taxes

Like sales taxes, excise taxes are usually collected by the seller from the buyer at the point of sale. However, an excise tax differs from a sales tax in three ways:

1. An excise tax applies to a narrow range of products, such as tobacco products. A sales tax applies to most goods and some services.
2. An excise tax is based on the number of units purchased, such as cartons of cigarettes or gallons of gasoline. A sales tax is based on the amount paid.
3. An excise tax is usually a much greater proportion of the total sales price than a sales tax.

Fuels used in farming are not subject to the federal excise tax that is collected on fuels used in vehicles driven on public roads. Farmers can claim a credit on their federal income tax returns for the excise taxes they paid when they purchased the gasoline if they use the gasoline for a farming purpose. If farmers purchase diesel fuel and use it for a farming purpose, they can either claim a credit on their federal income tax returns or file a refund claim for the excise taxes paid on the diesel fuel.

Cross-Reference

See Chapter 14 of IRS Publication 225, *Farmer's Tax Guide*, for more details on the excise taxes on gasoline and diesel fuel.

Gift Taxes

A gift tax is imposed on the value of gifts made during the donor's life. The federal government and several states collect a gift tax. The amounts that can be given tax-free and the gift tax rates vary from state to state. This brief overview discusses only the federal gift tax.

Annual Exclusion

The federal gift tax rules include an annual exclusion. For 2022, donors may exclude from the gift tax the first $16,000 given to each of any number of individuals. The $16,000 amount is adjusted for inflation, so it may be a different amount in future years, but it will always be an even multiple of $1,000. In addition to the $16,000 (as adjusted for inflation), payments for the benefit of another individual are excluded from taxable gifts if they are made directly to an institution of higher learning or to a person or entity that provides medical care to the individual.

Example 2.2: Gift Tax Annual Exclusion

Guaming Yang gave $116,000 to each of her three children in 2022, for a total of $348,000 being gifted. Guaming's taxable gifts for 2022 total $300,000. Since the first $16,000 transferred to each child is excluded from taxable gifts, that leaves $100,000 per grandchild as taxable for a total of $300,000.

Gifts Between Spouses

Gifts of any amount to the donor's spouse are excluded from taxable gifts. Therefore, spouses can give as much as they want to give to each other, and they will not be subject to the federal gift tax on those gifts. This is the unlimited marital deduction provision of the tax law.

Gifts to Charity

Gifts of any amount to qualified charities are excluded from taxable gifts. Therefore, an individual can reduce his or her taxable estate without paying any gift tax by making donations to qualified charities.

Federal Gift Tax Rate

The effective federal gift tax rate for taxable gifts in 2022 range from 18% to 40%. There are some very specific rules for various purposes that may require or exclude/exempt federal gift taxes from being owed. Please refer to the Instructions for IRS Form 709.

Applicable Exclusion Amount (Lifetime Exclusion Amount)

An applicable credit amount offsets the federal gift tax using the first $5,000,000 base that has increased for inflationary purposes. In December of 2017, the Tax Cuts and Jobs Act doubled the lifetime exclusion amount for a limited time. Beginning on January 1, 2026, the personal lifetime exclusion amount will again revert to the $5,000,000 base plus appropriate inflationary adjustments. The 2022 per person lifetime exclusion is $12,060,000. Unlike the annual exclusion, each donor has only one applicable exclusion amount for cumulative taxable gifts made to all donees. The applicable exclusion amount for gifts in any tax year is reduced by the donor's prior taxable gifts that were tax-free because of the gift tax applicable exclusion amount in effect at the time of the prior gifts.

Example 2.3: Gift Tax Applicable Exclusion Amount

John James made no taxable gifts before 2020, when he gave each of his three children $215,000. The 2020 annual exclusion was $15,000, which reduced each taxable gift to $200,000, for a total of $600,000 of taxable gifts. The $11,580,000 lifetime applicable exclusion amount for 2020 resulted in no gift tax on the $645,000 taxable gifts.

In 2021, John gave his children another $515,000 in taxable gifts for each of the three children for a $1,545,000. The annual exclusion amount for 2021 was also $15,000 which brings the total to $1,500,000 that is applied to the lifetime exclusion along with the $600,000 from 2020. The $11,700,000 applicable lifetime exclusion amount for 2021 is reduced by the $600,000 2020 gift and the $1,500,000 2021 gift. Therefore, $2,100,000 ($600,000 + $1,500,000) is subtracted from the $11,700,000 which leaves at least $9,600,000 that can be gifted or passed through the estate after John's death tax-free if John were to die before 2026.

If John provided only one gift in the year 2021, of $5,000,000 to each of the children then John would have exceeded his life-time exclusion amount by $3,300,000. The tax rate on the $3,300,000 is 40% since the value is above $1,000,000, which would equate to a gift tax of $1,320,000 that would need to be paid by John. For further details please see IRS Instructions for Form 709.

Planning Pointer

Opportunity in 2002 through 2025

Taxpayers may want to make gifts prior to 2026 to take advantage of the higher lifetime applicable exclusion amount. Congress could increase the applicable exclusion amount for 2026 and later years but that is not a guarantee. Pay attention to future legislation for any possible changes that may occur.

Estate Taxes

An estate tax is imposed on the value of a decedent's taxable estate. The federal government and several states collect an estate tax. The amounts that can be passed tax-free and the estate tax rates vary from state to state. This brief overview discusses only the federal estate tax.

Note

Rules are More Complex

The rules for computing the estate tax are more complex than this summary indicates, but this summary explains the effect of those tax rules. See IRS Publication 950, *Introduction to Estate and Gift Taxes*, and IRS Publication 559, *Survivors, Executors, and Administrators*, for more information on estate taxes.

Gross Estate

For purposes of the federal estate tax, a decedent's gross estate includes the value of all property the decedent owned—directly or indirectly—at the time of death. In addition to the decedent's tangible assets (such as cash, bank accounts, personal property, and real estate), the gross estate includes intangible assets (such as life insurance owned by the decedent) and annuities payable to the decedent or the decedent's heirs.

> **Note**
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> ***Probate Estate is Different***
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> Some assets that are excluded from a decedent's probate estate are included in the decedent's federal estate tax gross estate. For example, if the decedent owned a life insurance policy on his or her life and the proceeds are payable to a beneficiary other than the decedent's estate, the policy is excluded from the probate estate, but it is included in the federal estate tax gross estate.

Taxable Estate

A decedent's taxable estate is the gross estate reduced by deductions for debts owed by the decedent, funeral expenses, amounts going to a charity, and state death taxes. The value of the estate going to the spouse may not be taxable to the estate dependent on facts and circumstances. Present (2022) Estate and Gift Tax law allows for the deceased spouses' unused lifetime exclusion amount to be transferred to the surviving spouse; this is called "portability". Although gifts made while alive to a spouse are tax free, the overall value of the estate's assets is potentially taxable above the lifetime exclusion limit. Portability allows the unused portion of the deceased lifetime exclusion amount to be transferred to the spouse and added to the spouse's individual exclusionary amount. This does require tax form(s) to be filed within a specified period to make use of portability.

Applicable Exclusion Amount

An applicable credit amount offsets the federal estate tax on the first $12,060,000 of the taxable estate for deaths in 2022. The applicable exclusion amount is scheduled to be cut in half for deaths after 2025. The applicable exclusion amount is reduced by the donor's taxable gifts that were tax-free because of the gift tax applicable exclusion amount in effect at the time of the gifts.

Inheritance Taxes

An inheritance tax is imposed on a person who inherits property. There is no federal inheritance tax, but some states impose an inheritance tax on the value of money and other property that is inherited from a decedent.

Inheritance tax rules vary from state to state, but most states have an exemption amount that is not taxed and tax rates that increase as the amount that is inherited increases. Exemptions and rates often vary by the relationship of the heir or beneficiary to the decedent. An inheritance from a spouse might not be taxed, and an inheritance by a child might have a large exemption amount and low tax rates on the amount above the exemption amount. The exemption amount might decreas, and the tax rates increase for inheritances from more distant relatives, with the lowest exemption amount and the highest tax rates applying to an inheritance from an unrelated decedent.

Income Taxes

An income tax imposes a tax on the taxpayer's income. The federal government, most state governments, and some local governments collect an income tax. Many state and local income taxes are based on the federal income tax rules, with varying adjustments. This brief overview discusses only the federal income tax.

Figure 2.1 summarizes the income tax computation by outlining the steps taxpayers follow on Form 1040, U.S. Individual Income Tax Return.

Figure 2.1. Outline of Federal Income Tax Calculation

Gross Income
– Above-the-line deductions
= Adjusted gross income
– Standard deduction or itemized deductions
– Personal and dependent exemptions deduction (due to the Tax Cuts and Jobs Act, there are no Personal exemption deductions through the 2025 tax year).
= Taxable income
× Income tax rates
= Income tax
– Credits
+ Other taxes
= Total tax
– Tax payments during the tax year
= Tax due with return or tax refund

Gross Income

The Sixteenth Amendment to the United States Constitution gives Congress the power to collect taxes on income. Congress used that power by defining gross income as "all income from whatever source derived." Because of that broad definition, an increase in wealth is included in taxable income unless it is specifically excluded. For example, Congress excludes an increase in the value of property from gross income until there is a taxable event, such as a sale.

Form 1040 provides separate lines to report several categories of income, such as wages, interest, dividends, refunds, alimony, distributions from retirement plans, unemployment compensation, and social security benefits.

An individual's gross income from a sole proprietorship is reported on Schedule C (Form 1040), Profit or Loss From Business (Sole Proprietorship); Schedule E (Form 1040), Supplemental Income and Loss; or Schedule F (Form 1040), Profit or Loss From Farming. The related business expenses, which are some of the above-the-line deductions, are also reported on those forms. Only the net business income is reported on Form 1040.

Similarly, proceeds from selling assets that qualify for capital gain treatment are reported on Schedule D (Form 1040), Capital Gains and Losses. The income tax bases of those assets are also reported on Schedule D (Form 1040) and subtracted from the sale proceeds before the net amount is carried to Form 1040.

An individual's share of income from flow-through entities, such as partnerships, S corporations, and trusts, is reported first on Schedule E (Form 1040) and then carried to Form 1040.

Gross income that does not fall within any category on the itemized lines on Form 1040 is reported on a line called "Other income" (line 8 on the 2022 form).

Because deductions are subtracted from business income before it is reported on Form 1040, an individual's total gross income does not show up in any one place on the income tax return, and there is no line labeled "gross income." The sum of the income and losses that are reported in the income section of Form 1040 (line 9 on the 2022 form) is appropriately labeled "total income."

Adjusted Gross Income

Adjusted gross income (AGI) is an important number in the income tax calculation because it is used as a base for some other calculations. For example, medical expenses can be deducted only to the extent they exceed 7.5% of AGI. Most miscellaneous itemized deductions reduce taxable income only to the extent the total exceeds 2% of AGI.

AGI is calculated by subtracting any remaining above-the-line deductions from total income (business expenses and the bases of assets were already deducted on other schedules). The remaining above-the-line deductions include educator expenses, health savings account contributions, moving expenses, one-half of self-employment taxes, the cost of self-employed health insurance, certain retirement plan contributions, interest paid on student loans, deductible tuition and fees, and Section 199, 199a, etc.. Due to tax law changes, alimony may or may not be included as an above-the line deduction due to facts and circumstance primarily based on the date and the language of the divorce decree.

Including a deduction in the above-the-line category, rather than as an itemized deduction, has three effects on tax liability:

1. Above-the-line deductions can be claimed even if the taxpayer claims the standard deduction instead of itemizing deductions.
2. Above-the-line deductions are not subject to the floors that reduce some itemized deductions.
3. Above-the-line deductions reduce AGI, which affects other tax calculations as described earlier.

Standard Deduction

If a taxpayer does not elect to itemize deductions, he or she subtracts the standard deduction from AGI. Standard deductions vary by filing status, dependency status, and the taxpayer's age, and are increased for taxpayers who are legally blind.

Cross-Reference

See Figure 13.1 in Chapter 13 of this guide for a list of the 2022 standard deductions.

Itemized Deductions

Itemized deductions are personal expenses for which Congress specifically allows a deduction. They include medical and dental expenses (to the extent the total exceeds 7.5% of AGI); state and local taxes; interest on a home mortgage; gifts to charities; casualty and theft losses of property used for personal (rather than business) purposes; employee business expenses; investment expenses; and tax preparation expenses.

In most cases, taxpayers should elect to itemize their deductions if the total exceeds their standard deduction. However, a married person who files separately cannot itemize his or her deductions if his or her spouse claims the standard deduction.

Standard Deduction & Dependent Exemptions Deduction

Because of the Tax Cuts and Jobs Act of December 2017, there are no personal deductions allowed through tax year 2025. But there is an available deduction for some dependents of those taxpayers. The taxpayer (parents/guardians) are eligible for a standard deduction with a value determined by filing status. For example, a married couple with three children who file a joint income tax return can claim three dependent exemptions. For 2022, their standard deduction is $25,900, and dependent exemptions deduction is up to $1,150 for qualifying dependents. This would total a deduction of $29,350: ($25,900 + ($1,150 x 3)).

Taxable Income, Income Tax Rates, and Income Tax

Taxable income is the remainder after itemized deductions or the standard deduction and the personal (following 2025 tax year) and dependent exceptions deduction are subtracted from AGI. It is the base to which the tax rates are applied to compute income tax liability.

The income tax rates are graduated, which means that a higher tax rate applies to higher levels of income. The higher rates apply only to the income above the threshold for each rate and not to the income below that threshold.

Example 2.4: Income Tax Rates

Victor and Maria Gomez reported $150,000 of taxable income on their 2021 joint income tax return. For 2021, the joint return tax rate on the first $19,900 of taxable income is 10%. The tax rate for the next $61,150 is 12% and the final $68,950 is taxes at a rate of 22%. Therefore, the Gomezes' 2021 income tax is $24,497, as shown below.

Tax on first $19,900 of taxable income ($19,900 × 10%)		$1,990
Tax on amount over $19,900		
12% tax bracket: $81,050 - $19,900 =$61,150	$61,150 * 12%	$7,338
22% Tax bracket: $150,000 - $81,050 = $68,950	$68,950 * 22%	$15,169
Total tax		$24,497

The federal income tax rate on long-term capital gains and qualified dividends is the lesser of the ordinary income tax rate or the tax rate for long-term capital gain. For 2022, the tax rate for most long-term capital gains is 0% for eligible gains and dividends included in total taxable income that does not exceed the $83,350 for Married Filing Jointly (MFJ) filed returns or $41,675 for single individuals. It is 15% for eligible long-term capital gains and dividends included in income that would be above $83,350 for MFJ filed returns or above $41,675 for single filers.

Figure 2.2. 2022 Long Term Capital Gain Rates

2022 Long Term Capital Gains Rates	Single/Individual		Married Filing Jointly		Head of Household	
	Above	Top	Above	Top	Above	Top
0%	$ -	$ 41,675.00	$ -	$ 83,350.00	$ -	$ 55,800.00
15%	$ 41,676.00	$459,750.00	$ 83,351.00	$ 517,200.00	$ 55,801.00	$ 488,500.00
20%	$459,751.00	And Up	$517,201.00	And Up	$ 488,501.00	And Up

*There are higher capital gain rates for collectibles. Long-term capital gains for C-corporations are treated at the same tax rate as ordinary income.

Example 2.5: Tax Rates for Capital Gain

In 2022, Victor and Maria Gomez have $25,000 of long-term capital gains, in addition to $80,000 of ordinary income. The top of the 0% tax rate for long-term capital gain is $83,350 (total of ordinary income and capital gain income) for married filing jointly; any gain that falls above that amount will be treated at a 15% tax rate until $517,200 of total income, where a 20% tax rate will be applied.

The Gomez's have $80,000 of ordinary income and $25,000 of long-term capital gain income. Since the $80,000 of ordinary income is below the $83,350 (see below) there is $3,350 of the long-term capital gain income that will be taxed at a 0% tax rate and the remaining long-term capital gain income will be taxed at a 15% tax rate since it is below the $517,200.

Ordinary Income ($80,000**)**		
Tax on Ordinary Income		
$20,550 at 10% (of the $80,000)	$2,055.00	
$59,450 at 12% ($80,000 - $20,550)	$7,134.00	
Total Tax Owed on Ordinary Income	$9,189.00	$9,189.00
Long-Term Capital Gain (LTCG) ($25,000)		
$3,350 of capital gain ($83,350 – $80,000) = ($3,350 * 0%)	$0.00	
$21,650 ($25,000 - $3,350) * 15%	$3,247.50	
Total Tax Owed on Long-Term Capital Gain	$3,247.50	$3,247.50
Total of all Taxes Owed ($3,247.50 LTCG + $9,189 Ordinary Inc):		$12,436.50

Credits

If the alternative minimum tax (see Chapter 9 of this guide) is owed, it is added to the income tax liability before nonrefundable credits are subtracted. These credits include the foreign tax credit; the credit for child and dependent care expenses; education credits, such as the Hope credit and the lifetime learning credit; the retirement savings contribution credit; the child tax credit; residential energy credits; and others.

The order in which credits are subtracted is important because some credits are refundable and some are not. If the amount of tax due before a refundable credit is applied is less than the refundable credit, the excess amount of the credit can be received as a refund. By contrast, if a nonrefundable credit exceeds the amount of tax due, the credit can be used only to reduce the tax to zero. The excess is not refundable.

Observation

Benefit of Credits

Because tax credits offset tax liability, the benefit of a credit is the same for both high- and low-bracket taxpayers if there is a tax liability for the credit to offset or if the credit is refundable. By contrast, the benefit of a tax deduction depends on the tax bracket of the taxpayer. A $100 deduction from income in the 35% bracket saves the taxpayer $35 of taxes. A $100 deduction from income in the 12% bracket saves the taxpayer $12 of taxes.

Other Taxes

Taxes that cannot be reduced by nonrefundable credits are added to the net tax due after the credits are subtracted. These taxes include the self-employment tax; social security and Medicare taxes that were not already paid on tips and wages; and other taxes.

Total Tax, Tax Payments, and Tax Due

Payments include withholding and estimated payments and refundable credits. They are subtracted from the total tax liability to arrive at the tax balance that is due with the return or the tax refund that the IRS will send to the taxpayer.

Employment Taxes

Most wages paid to employees are subject to Federal Income Contributions Act (FICA) taxes and Federal Unemployment Tax Act (FUTA) taxes.

Cross-Reference

See Chapter 13 of IRS Publication 223, *Farmer's Tax Guide*, for more information on FICA and FUTA taxes.

FICA Taxes

Both the employer and the employee must pay FICA taxes on the employee's wages.

The FICA tax is comprised of two taxes. One is the social security tax (also called old-age, survivors, and disability insurance), which funds social security benefits, including disability, retirement, and survivor benefits. Since 1990, the social security tax rate has been 6.2% for both the employer and the employee. The social security tax applies only up to an inflation-adjusted wage base, which is $147,000 for wages paid in 2022.

The second tax included in FICA taxes is the Medicare tax (also called hospital insurance), which funds Medicare payments. Since 1986, the Medicare tax rate has been 1.45% to be paid by the employer and 1.45% paid by the employee for a total of 2.9%.

Unlike the social security tax, there is no wage limit for the Medicare tax. Employers and employees owe this tax on all of wages paid/received.

Combined, the social security tax and the Medicare tax impose a 7.65% tax on both employers and employees for the first $147,000 (for 2022) of wages. There is an additional 0.9% Medicare Tax for those that that earn above $200,000, this is to be paid by the employee not the employer.

Employers must withhold the employee's share of FICA taxes from wages and remit both the employee's share and the employer's share to the United States Treasury. Employers then report the wages and taxes on employment tax returns filed with the IRS.

FUTA Taxes

Farmers must pay FUTA taxes if they meet either of the following tests:

1. They pay $20,000 or more to farmworkers in any calendar quarter during the current or preceding calendar year, or
2. They employ 10 or more farmworkers for at least some part of a day during any 20 or more different calendar weeks during the current or preceding calendar year.

FUTA is paid only by the employer, not the employee. There are some limitations, such as being able to subtract from the federal percentage of 6% (for 2022) on the first $7,000 (for 2022) of wages by taking a credit for State Unemployment funds paid, up to a limit of 5.4% for 2022. The caveat to this is "as long as the state that SUTA was paid into is not determined to be a credit reduction state". Please see IRS Instructions for Form 940.

Noncash Wages

Noncash wages paid to farmworkers may not be subject to FICA or FUTA taxes. Noncash wages include food, lodging, clothing, transportation passes, commodities, and other goods and services. There are some very specific rules that must be followed especially if products, such as grain or livestock, are being used as wages for it to not be subject to FICA and FUTA. Further details can be found in Chapter 3 Wages and Other Compensation within IRS publication 51 (Circular A), Agricultural Employer's Tax Guide

Planning Pointer

Social Security Benefits

Paying noncash wages to farmworkers may save FICA taxes for both the employer and the employee and may save FUTA taxes for the employer. However, noncash wages are not counted as earned income for calculating social security benefits. Therefore, employers and employees should compare the FICA and FUTA taxes saved with the social security benefits lost by paying noncash wages.

Self-Employment Taxes

Instead of paying FICA taxes on wages, self-employed individuals pay self-employment tax on their self-employment income. Like the FICA tax, the self-employment tax is comprised of the social security tax and the Medicare tax. The social security and Medicare tax rates equal the sum of the rates paid by the employer and the employee on wages. Therefore, the self-employment tax rate is 12.4% and the Medicare tax rate is 2.9%, for a total of 15.3%.

The wage base that limits the social security tax to the first $147,000 (for 2022) of wages also limits the social security component of the self-employment tax to the first $147,000 (for 2022) of self-employment income. If a taxpayer receives both wages and self-employment income, the base for self-employment taxes is reduced by the wages he or she receives.

Cross-Reference

See Self-Employment section/chapter of IRS Publication 225, *Farmer's Tax Guide*, for more information on the self-employment tax.

Summary

Farmers must pay several different taxes that vary in their complexity and the way they are collected. Effective farm management includes minimizing taxes. However, some taxes are easier to manage than others. It is highly recommended that each farmer and rancher is able to have a tax professional that is familiar with agricultural taxation and that a tax management strategy meeting is held at least 30-60 days prior to the conclusion of the tax year.