

## Tax Planning for Farmers\*

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### Introduction

Farm income can vary greatly between high-income years and low-income years. Variations of yields, prices, and input costs impact year-to-year taxable income and tax due. There are unique tax provisions for farming and ranching that provide flexibility to manage taxes through planning. This article provides an overview of tax management and planning concepts, plus where to find additional information. While there are several types of taxes that are paid and can be included in tax planning, this article will focus primarily on federal income tax. This article provides a general overview of the concepts of tax planning and prepares you for discussions with your tax advisor. At the end of this article is a list of other topics that will provide more information on topics introduced in this article, including Managing Income Taxes Before Year-End and Managing Income Taxes After Year-End.

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## Why Tax Planning?

The goal of tax planning is to smooth taxable income over multiple years to result in maximizing after-tax net income. In general, it is using the provisions available to move when income is recognized or when deductions are taken, allowing the business owner to use the lower tax rates and avoid being subjected to the significantly higher tax rates.

There are a couple of items to keep in mind. Taxable income is more than just *Schedule F (Form 1040), Profit or Loss From Farming*. Sales of breeding livestock and farm equipment is found on *Form 4797, Sales of Business Property*. There may be income for farming on other forms or schedules. Additionally, tax planning incorporates non-farm income, such as income from wages, interest, and dividends.

**Note.** In general tax planning does not eliminate tax; it is more about either accelerating (recognizing in an earlier year) income or expenses, or deferring income or expenses to a future year. By its nature, the consequences of tax planning affect multiple years' taxable income and should be carefully considered with a tax professional. The goal of tax management is to maximize after-tax net income over the life of the business, not to minimize taxes paid.

When considering whether to buy equipment, the overall needs of the operation, cash flow, and other considerations should be used in making purchase decisions. Tax planning is used to make decisions about the timing of the purchase and the use of various depreciation methods that would have a larger or smaller portion deducted or written-off in the year of the purchase. It never makes sense to buy equipment only for the tax deduction.

## General Tax Overview

This is a general overview of how tax rates are applied to federal taxable income. Following is a general list of terms used when determining taxable income and calculating the amount of income tax due:

- **Gross Income:** Sum of income from all sources and schedules (i.e. net profit from farming, wages and tips).
- **Adjusted Gross Income:** Gross Income less adjustments (i.e. half of self-employment taxes)
- **Taxable Income:** Adjusted Gross Income less standard or itemized deduction. For 2025, the standard deduction is \$15,000 for single taxpayers.
- **Tax (before credits and payments):** The tax brackets are used to calculate the tax. Lower rates are first applied, and then any additional income is taxed at a higher rate. These rates are referred to as the marginal tax rate, or the rates at which additional taxable income will be taxed.

- Tax Credits: Specific provisions for various tax credits (i.e. child tax credit).
- Taxes Owed: Tax (before credits and payments) less tax credits.
- Tax Due: Taxes owed less payments made.

**Table 1. Tax brackets for marginal tax rates on taxable income, single filing status, in 2024 and 2025.**

Tax rate	2024 Taxable Income	2025 Taxable Income
10%	\$1 – 11,600	\$1 – 11,925
12%	\$11,601 – 47,150	\$11,926 – 48,475
22%	\$47,151 – 100,525	\$48,476 – 103,350
24%	\$100,526 – 191,950	\$103,351 – 197,300
32%	\$191,951 – 243,725	\$197,301 – 250,525
35%	\$243,726 – 609,350	\$250,526 or more
37%	\$609,351 or more	

**Example 1:**

Ima Farmer had an adjustable gross income of \$88,850 for 2025. Ima used the standard deduction of \$15,000. Her federal taxable income is the adjusted gross income, less the standard deduction: \$88,850 - \$15,000 = \$73,850. The tax brackets are used to calculate the taxes. The first \$11,925 is taxed at 10%, the next \$36,550 is taxed at 12%, and the remaining \$25,375 is taxed at 22%. The total is \$11,161.

Tax rate	Taxable Income	Ima's Income	Ima's Tax based upon each Marginal Tax Rate
10%	\$1 – 11,925	\$11,925 * 10%	\$1,193
12%	\$11,926 – 48,475	\$36,550 * 12%	\$4,386
22%	\$48,476 – 103,350	\$25,375 * 22%	\$5,583
	<b>Total</b>	<b>\$73,850</b>	<b>\$11,161</b>

Tax planning could help Ima smooth her income and avoid higher tax brackets in high income years by recognizing more income in low-income years. It is better to pay income tax at lower rates such as 10% and 12%, rather than 22%, 24% or more in a later year.

Note: This example calculation is only for federal income tax. Self-employment tax is typically 15.3% of net income from a farm or business, and there may be additional state and local taxes.

## Tax Planning Strategies

As mentioned above, tax planning is using the flexibility available in the tax code. There are nuances, facts, and circumstances that will affect the ability to use these tax management tools in individual

situations. Below is an overview of the general concepts. Individuals should consult with their tax professional in developing a tax plan for their unique situation.

## Strategies for High Income Years

In years where income is higher than normal, tax management strategies and planning is used to reduce the taxable income for the current year to avoid the peaks resulting in higher marginal tax rates. This includes using tax provisions and tools to defer recognition of income to a future year, and using more deductions in the current year.

- **Deferring Recognition of Income.** This can be done through waiting to sell farm production until the following year. For example, grain may be harvested in fall of 2025 and stored to sell in the first part of 2026. If the farm is filing their tax return on a cash basis, the income is on the tax return for the year in which it is sold, not the year it is produced. By storing farm commodities, the farm is deferring the income from the 2025 grain until 2026. Additional provisions may include installment sales.
- **Recognizing Expenses in the Current Year.** These strategies are meant to show a higher deduction in the current taxable year for expense. For example, an expense such as fertilizer is purchased in 2025 to be used in 2026. This will result in higher expenses for 2025, and hence lower taxable income. Other options include using provisions that show higher depreciation in the current year.

## Strategies for Low Income Years

In years where farm income is lower, tax planning can be used to increase the current year's taxable income. This reduces income that would be recognized in a future year and keeps income consistent across the years resulting, in lower overall marginal rates.

- Recognizing more income
- Deferring expenses

## How It Is Done

Effective tax planning requires good records and consultation with a tax professional before the end of the year to determine the timing of some transactions (i.e. before the end of the year or waiting until the following year). It is important to carefully consider the provisions to use after the end of the year in preparation of the tax return. Many of these choices will affect more than one year's taxable income and tax owed.

It should be noted that deferring taxes does not mean they are eliminated. The taxes will still be owed in a future year. Excessive use of deferment over many years can result in a large tax burden as the operation is considering transitioning or ending the operation.

## **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.

Additional resources that can be used in developing a tax plan and learning more about the concepts for RuralTax.org include:

- How to Choose a Tax Professional
- Working with a Tax Professional
- Managing Income Taxes Before Year-End
- Managing Income Taxes After Year-End
- Depreciation
- Net Operating Loss

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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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