Farm Tax Workshop
December 13, 2021

Sarah Burnett Pierce grew up on a mid-sized farm in northwest Missouri with cow-calf, farrow-to-finish, dairy, row crop and pastured poultry operations. Sarah's Masters of Accountancy is pending completion and she holds a B.S. in International Ag. Development and an A.A. in Farm & Ranch Management. After spending 11 years in supportive roles in the tax and accounting industry, she obtained her Enrolled Agent Certification in 2017. She owns Moxie Tax Solutions north of Richmond, MO and specializes in farm, small business & individual taxes. Sarah is focused on assisting clients in understanding their taxes, furthering her own tax education and managing her growing Katahdin sheep flock.
Types of Tax Preparers

Paid Tax Preparer

- No training or education required
- Registered for ID# (PTIN) with IRS
- Optional Annual Filing Season Program (AFSP) registration - can represent some client’s issues before IRS

Enrolled Agent

- Registered for ID# (PTIN) with IRS
- Scored 80% or higher on the 300 question certification exam
- Passed the IRS Suitability Screening for tax compliance
- Completes an average of 24 hours of CE each year - tax focus

Certified Public Accountant

Tax Lawyer
Types of Tax Preparers

Certified Public Accountant
- Requirements vary by state - Missouri & Kansas are very similar
- Bachelor’s Degree in Accounting
- Score 75% or higher on the 307 question CPA exam
- Score 90% or higher on the CPA Ethics Exam
- One year of full-time accounting experience
- Completes an average of 40 hours of CE each year - accounting focus

Tax Lawyer
- Juris Doctor Degree
- Pass State Bar Exams - Missouri & Kansas are very similar
  - Three section exam including 200 multiple-choice questions, essays and practical performance tasks
  - Minimum score in Missouri is 65% and Kansas is 67%
- Completes 15 hours in Missouri and 12 hours in Kansas of CLE each year

Which type of tax preparer do I need?
It depends…..

- Good & bad preparers in every group
- Price can be a factor
- Are your tax needs routine or do you have a larger issue to address?
- Do you need representation before the IRS?
- Choose someone you are comfortable with and you feel you can trust

Question submitted earlier:

How to find a tax professional experienced in farm taxes?

- Specialization is often more important than credentials
- Referral from a trusted individual is often a good place to start
- Most tax preparers will offer a free one-hour consultation - ask about number of farm clients, size of farms and how many years of experience with farm taxes
- It is easier to find an experienced, farm tax preparer in smaller, rural towns than in the cities
- Choose someone you are comfortable with and you feel you can trust
Any additional questions about tax preparers?

Is this a hobby or a business?
Consider the 9-Factor Test

1. Is the activity conducted in a businesslike manner and are complete and accurate books and records maintained?
2. Are there personal motives in carrying on the activity?
3. Does the time and effort put into the activity indicate a profit motive?
4. Is the taxpayer dependent on income from the activity?
5. Are losses due to circumstances beyond the taxpayer’s control (or are normal in the startup phase of the type of business)?
6. Is the taxpayer knowledgeable or do they have advisors necessary to carry on the activity as a successful business?
7. What is the taxpayer’s history of success in making a profit with similar activities in the past?
8. Is the activity profitable some years and how much is the profit?
9. Does the taxpayer expect to make a future profit from the appreciation of the assets used in the activity?

The 9-Factor test is a very bureaucratic way of asking:

Is the primary purpose to make a profit?

Joint Sheep Flock:
- Motivation is to make a profit
- Profits are used for living expenses
- Detailed records are kept for breeding, sales, expenses, assets, etc.
- Routine time and effort are spent to make the endeavor successful
- Plan in place for expansion

Jim’s Horses:
- Motivation is enjoyment
- Expense records are kept
- No effort to produce income
- Sporadic time and effort is spent
Why does it matter?

Income is reported for both a hobby and a business.

Hobby expenses reported cannot exceed income reported - cannot claim a loss on the tax return.

Business expenses reported can exceed income reported - can claim a loss on the tax return.

Claiming a loss will reduce total taxable income on the tax return, thus reducing taxes owed.

Any additional questions about hobby vs business?
Do I need an LLC?

It depends….

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<tr>
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<tr>
<td>LLC Choices</td>
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<td>SM LLC (default disregarded)</td>
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<td>C corporation rules</td>
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<tr>
<td>S corporation</td>
<td>S corporation rules</td>
</tr>
</tbody>
</table>

Liability is limited to the extent of the business investment. If the business loses a lawsuit or has other debt, the judgment is against the business and not its owners. Judgment is enforceable against the business, but not the owner’s other assets.
To LLC or Not
(This is not legal advice, it is a story of our business operations.)

Sarah & Jim’s Farm
Of The Earth Farm Distillery

Qualifying Joint Venture
LLC taxed as Partnership
Any additional LLC questions?

We will discuss each business structure and their tax implications next....

Common Farm Business Structures

- Sole Proprietor
- Qualifying Joint Venture
- Partnership
- S-Corp
- Corporation
Sole Proprietor

- One person
- Does not require any formal business structure documents
- Is always taxed as a Sole Proprietor by filing a Schedule F with their 1040 tax return
- Is classified as a Pass Through Entity - business does not pay the taxes, individual pays the taxes
- Individual's taxes are determined by the amounts on the Schedule F
- Can choose to form a Single Member LLC for additional liability protection, but tax treatment will not change

Qualifying Joint Venture

- Married couple both materially participating in the farming operation
- Does not require any formal business structure documents
- Is always taxed on a Married Filing Joint tax return by filing a Schedule F with their 1040 form - one Schedule F for each spouse
- Is classified as a Pass Through Entity - business does not pay the taxes, individual pay the taxes
- Each spouse’s taxes are determined by the amounts on the Schedule F
- CANNOT form an LLC for additional liability protection
Partnership

- Two or more people
- Should have formal business structure documents
- Is always taxed as a Partnership by filing 1065 tax return with a Schedule F attached - due March 15
- Is classified as a Pass Through Entity - business does not pay the taxes, individuals pay the taxes
- Individual’s taxes are determined by the information on the K-1
- Can choose to form an LLC for additional liability protection, but tax treatment will not change
- LLC formation requires an Operating Agreement

S-Corp

- File Articles of Incorporation with Secretary of State
- Create Bylaws by which the business will operate
- Must adhere to certain formalities and activities outlined by state statues or S-Corp status can be revoked - including “reasonable salary” for Officers
- Separate legal existence and liability protection with or without forming an LLC
- One to 100 Shareholders
- Must request S-Corp election on first tax return filed by the business
- Is always taxed as an S-Corp by filing 1120-S tax return with a Schedule F attached - due March 15
- Is classified as a Pass Through Entity - business does not pay the taxes, individuals pay the taxes
- Individual Shareholder’s taxes are determined by the information on the K-1
Corporation

- File Articles of Incorporation with Secretary of State
- Create Bylaws by which the business will operate
- Must adhere to certain formalities and activities outlined by state statues or Corporation status can be revoked
- Separate legal existence and liability protection with or without forming an LLC
- Unlimited number of Shareholders
- Is always taxed as an Corporation by filing 1120 tax return with a Schedule F attached - due April 15
- Is classified as a separate Entity - business pays taxes AND individuals pay taxes
- Individual Shareholder’s taxes are determined by the information on the K-1

Question submitted earlier:

We are currently an LLC taxed as a partnership. I’m wondering at what point an S-Corp makes more sense.

- Do you need the maximum amount of personal asset protection available?
- Are you planning to seek substantial investment from outsiders?
- Do you plan to become a publicly traded company?
- Is your farm profitable enough to pay each Officer a “reasonable salary”?
- There can be some tax advantages (discussed later), but the farm needs to be financially stable and reasonably profitable
- Are you prepared to create and follow the formal business activities and records outlined by state statues - annual meeting minutes, elected board of directors, payroll, etc.?
Any additional questions on common farm business structures?

Cash vs Accrual

**Cash Basis Accounting**
- Record revenue and expenses when the money is exchanged
- Does not track accounts receivable or accounts payable
- Can provide an inaccurate financial picture
- Matches income tax reporting method
- Recommend evaluating P&L by crop outside of formal books

**Accrual Basis Accounting**
- Record revenue and expenses when they are earned or incurred, not when the money is exchanged
- Provides an accurate picture of when money is earned and spent
- Required for companies with sales over $25 million
- Financial records can be converted prior to tax preparation
Benefit of Evaluating Profit & Loss by Crop Example

December 2019 two rams bred 78 ewes - breeding, vet feed, supply expenses
Jan-Apr 2020 care of 78 ewes during gestation - vet, feed, supply expenses
May-June 2020 78 ewes had 101 lambs - vet, feed, supply expenses
July - Oct 2020 care of 78 ewes & 101 growing lambs - vet, feed, supply expenses
Oct 2020 sell 25 lambs at 50-70# live wt. - sales income, commission expense
Nov 2020 - Mar 2021 care of 78 ewes & 76 lambs - vet, feed, supply expenses
Apr 2021 sell 76 lambs at 100-110# live wt. - sales income, commission expense

-----One crop has financial activity over three years of financial reports-----

Any additional questions on Cash Basis vs Accrual Basis?
Keeping Records

- There is no one correct method.....but, don’t use the truck dashboard! ☺
- Bookkeeping software - expense limitations and training requirements. Provides ease in recording the activities of more complex operations. Allows the farmer to analyze financial statements and reports.
- Excel spreadsheets - create income, expense and asset categories. Simple, straightforward approach to records. Categories can be totaled at year-end and provided to tax preparer. Additional spreadsheets may be created for financial analysis and internal reporting.
- Ledgers can more time consuming for data entry, but also provide sufficient information for tax purposes.
- Bookkeeping services - higher out-of-pocket cost, provides some guidance, relieves the need for software and/or training, access to financial reports
- Keep all receipts (legible), sales records, bank statements and financial documents for 7 years.
- Do data entry regularly to keep up-to-date
- Most tax preparers only want to see category totals. They are not auditing your records, they are completing forms to report your records.

Basic Checklist for the Schedule F

- Income total from items you raised
- Income total from items you purchased and resold
- Expense total for items purchased for resale
- Any 1099-NEC received for farm labor
- Any 1099-MISC received for rent or other miscellaneous farm income
- Any 1099-G received for government payments
- Expense totals for each applicable category on the Schedule F
- Expenses totals outside of these categories
- Purchases of equipment, buildings, breeding animals, fruit trees, computers, vehicles and other assets over $2500 provide: date of purchase, purchase price, percent used in business for depreciation
- Any 1099-NEC or 1099-MISC issued by the farming business
SCHEDULE F
(Form 1040)

Profit or Loss From Farming

Department of the Treasury
Internal Revenue Service

2020

Profit or Loss From Farming

A Principal crop or activity

B Enter code from Part IV

C Accounting method:

D Employer ID number (EIN) (see indir)

12/12/2021

For Department Use Only. Use the separate instructions. (Form 1040)

Social security number (SSN)
Do I need an EIN?

- Required if have employees and must issue W-2s
- Optional if you are issuing 1099-MISC or 1099-NEC
- Partnerships, S-Corp and Corporations must have one
Income Category Examples & Explanations

1. Produce to resell, feeder pigs sold as fat hogs, feeder calves sold as retail cuts. This does not include Value-added products. Final sale price MINUS cost of purchase goes in 1c.

2. Produce grown on the farm and animals born on the farm

3. Applies to large farm Cooperatives only

4. CRP, CSP, EQIP (high tunnels) and other USDA program payments - most are taxable

5. Deals with pledging a commodity as collateral for a government loan

6. COVID disaster payments reported to you on 1099-G

7. Farmer was paid to disc, seed, till, combine, etc.

8. Grant income - taxable. Fuel on a farm for farming purposes. Refund rate is $0.183/gallon. Can only claim refund for $750 or more. ($750/$0.183=4,098.36 gallons).

9. Gross income...

A Note on Value-added Products

- Processing is considered part of farming only to the extent that it is normally incidental to the growing, raising, or harvesting of commodities. This includes the washing, handling, packing, grading, or storing on a farm of any agricultural or horticultural commodity in its unmanufactured state.

- Drying, chopping, canning, juicing, fermenting that goes beyond incidental is not a farming activity and will be reported on Schedule C

- The farm “sells” products to the value-added enterprise and records this amount in income

- The value-added enterprise records this “purchase” as an expense on Schedule C, along with all other income and expenses related to the enterprise

- A written record should be kept for these transactions

- Accurate reporting is important because farmers receive some special tax treatments and some USDA/FSA and other farm programs are based solely on farm income or expenses

- To be safe, a farmer should determine if their farm liability insurance policy and/or any LLC that has been formed for the farming operation will provide adequate liability coverage for these types of activities
A Note on Agri-tourism

- Weddings, tours, educational classes, farm-to-table cooking events, hayrides, corn mazes, speaking engagements, etc. are not farming activities and should not be reported on Schedule F
- Income and expenses from these activities should be reported on Schedule C
- The Agri-tourism enterprise can “pay” rent to the farm, purchase produce, flowers, straw, etc. for events
- The farm reports these “sales” as income on Schedule F
- The Agri-tourism enterprise reports these “purchases” as expenses on Schedule C
- A written record should be kept for these transactions
- To be safe, a farmer should determine if their farm liability insurance policy and/or any LLC that has been formed for the farming operation will provide adequate liability coverage for these types of activities

Any Questions on Schedule F Part 1
Value-added or Agri-tourism?
Expense Category Examples & Explanations

10. Parking fees, tolls, actual operating expense or standard mileage rate of $0.56
11. Chemicals...
12. Soil or water conservation expenses (unless added to the basis of the land) and endangered species recovery
13. Hired someone to perform machine work for you (discing, seeding, planting, etc.)
14. Depreciation...
15. Examples: accident and health plans, group-term life insurance, and dependent care assistance programs for employees and dependent care assistance programs for the self-employed farmer
16. Feed...
17. Fertilizer and lime...
18. Freight and trucking...
19. Gasoline, fuel and oil...
Expense Category Examples & Explanations

20. Insurance...
21. Interest...
22. Labor hired...
23. Contributions to employee pension, profit-sharing, or annuity plans. Self-employed farmer contributions go on Schedule 1.
24. Land, machinery, equipment, vehicles leased for less than 30 days
25. Repairs and maintenance...
26. Seeds and plants... (not fruit trees or vines)
27. Storage and warehousing...
28. Supplies...
29. Real estate and personal property taxes for the farm, employer portion of Social security and Medicare and federal unemployment tax and state unemployment insurance withheld on employees’ wages, or federal highway use tax (55,000# or more). Tell tax preparer about ANY taxes you paid.

Any Questions on Schedule F Part 1
Value-added or Agri-tourism?

We will discuss depreciation, business use of home and labor in more detail next....
More on Depreciation

- If you buy or make improvements to farm property with a useful life of more than one year, you cannot deduct the entire cost in that year.
- Instead, the cost is spread over the IRS determined useful life of the item.
- Land is not depreciated - considered to have an indefinite useful life.
- Recent tax acts have greatly increased the bonus depreciation options - much larger portions can be taken in the first year. Not always a prudent choice.
- The date purchased or date the property is ready for use is used to determine the part-year depreciation amount.
- Basis for depreciation is usually the purchase price multiplied by the percent of business use.
- Most farmers use the GDS recovery periods under MACRS. (General Depreciation System and Modified Accelerated Cost Recovery System)

Table 7-1. Farm Property Recovery Periods

<table>
<thead>
<tr>
<th>Assets</th>
<th>GDS</th>
<th>ADS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agricultural structures (single purpose)</td>
<td>10</td>
<td>15</td>
</tr>
<tr>
<td>Automobiles</td>
<td>5</td>
<td>5</td>
</tr>
<tr>
<td>Calculators and copiers</td>
<td>5</td>
<td>7</td>
</tr>
<tr>
<td>Cattle (dairy or breeding)</td>
<td>7</td>
<td>7</td>
</tr>
<tr>
<td>Communication equipment</td>
<td>5</td>
<td>5</td>
</tr>
<tr>
<td>Computer and peripheral equipment</td>
<td>5</td>
<td>5</td>
</tr>
<tr>
<td>Driveway facilities</td>
<td>15</td>
<td>20</td>
</tr>
<tr>
<td>Farm buildings</td>
<td>20</td>
<td>26</td>
</tr>
<tr>
<td>New farm machinery and equipment</td>
<td>9</td>
<td>10</td>
</tr>
<tr>
<td>Used farm machinery and equipment</td>
<td>7</td>
<td>10</td>
</tr>
<tr>
<td>Fences (agricultural)</td>
<td>7</td>
<td>10</td>
</tr>
<tr>
<td>Goats and sheep (breeding)</td>
<td>5</td>
<td>6</td>
</tr>
<tr>
<td>Grain bins</td>
<td>7</td>
<td>10</td>
</tr>
<tr>
<td>Hogs (breeding)</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>Horses (age when placed in service)</td>
<td>7</td>
<td>10</td>
</tr>
<tr>
<td>Breeding and working (12 years or less)</td>
<td>3</td>
<td>10</td>
</tr>
<tr>
<td>Breeding and working (more than 12 years)</td>
<td>9</td>
<td>12</td>
</tr>
<tr>
<td>Horticultural structures (single-purposed)</td>
<td>10</td>
<td>15</td>
</tr>
<tr>
<td>Logging machinery and equipment</td>
<td>5</td>
<td>6</td>
</tr>
<tr>
<td>Nonresidential real property</td>
<td>30</td>
<td>40</td>
</tr>
<tr>
<td>Office furnitures, fixtures, and equipment</td>
<td>7</td>
<td>10</td>
</tr>
<tr>
<td>Paved lots</td>
<td>16</td>
<td>20</td>
</tr>
<tr>
<td>Residential rental property</td>
<td>27.5</td>
<td>40</td>
</tr>
<tr>
<td>Tractor units (over-the-road)</td>
<td>0</td>
<td>4</td>
</tr>
<tr>
<td>Tractors or tractors (trucks or similar)</td>
<td>10</td>
<td>20</td>
</tr>
<tr>
<td>Truck (tires only, excluding weight 15,000 lbs. or more)</td>
<td>5</td>
<td>5</td>
</tr>
<tr>
<td>Truck (combined weight less than 15,000 lbs.)</td>
<td>5</td>
<td>5</td>
</tr>
<tr>
<td>Water wells</td>
<td>15</td>
<td>20</td>
</tr>
</tbody>
</table>
Question submitted earlier:

Do urban farmers claim depreciation expenses in the same way that other farmers do?

- Yes
- All business owners in every industry adhere to the IRS regulations on depreciation
- The regulations are very specific and provide few options for adjustments
Question submitted earlier:

Can you depreciate a barn remodel?

Remodel or Renovation

► Restoration or significant improvement
► Involve major components or substantial structural parts of the building
► Construction that furthers the useful life of the property
► Roofs, windows, doors, gutters, interior walls, flooring, support beams, etc.

Repairs & Maintenance

► Routine maintenance on small components of the building
► Superficial improvements
► Install new door knob, paint, screen repair, replace missing floor boards or roof shingles
► Small components or improvements that are part of a larger remodel project are depreciated as part of that project - door knob installed in a new interior wall is part of the wall project

Any additional depreciation questions?

We will discuss business use of home and labor in more detail next....
More on Business Use of Home

- Part of your home is used exclusively & regularly by farm
  - Exclusively = cannot be used for ANY other purpose
  - Regularly = cannot be incidental or occasional use

**MUST BE USED FOR:**
- Principal place of business - can have more than one business location, BUT cannot have any other fixed location where you conduct substantial administrative or management activities
  - AND/OR
- A place to exclusively & regularly meet with customers in the normal course of business
  - AND/OR
- Other exclusive or regular business activity in a separate structure that is not attached to your home - garage, greenhouse, storage shed, barn

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**Figure A. Can You Deduct Business Use of the Home Expenses?**

Do not use this chart if you use your home for the storage of inventory or product samples, or to operate a daycare facility. See Exceptions to Exclusive Use, earlier, and Daycare Facility, later.

1. **Start Here:**
   - Is part of your home used in connection with a trade or business?
     - Yes
     - Are you using the part of your home as an employee?
       - No
       - **Is the use regular and exclusive?**
         - Yes
         - Is it your principal place of business?
           - Yes
           - Do you meet patients, clients, or customers in your home?
             - Yes
             - Deduction allowed
             - No
             - Is it a separate structure?
               - Yes
               - Deduction allowed
               - No
               - **No deduction unless inventory & samples**
     - No

2. **No deduction unless inventory & samples**
More on Business Use of Home

Actual Expenses

- Deduct 100% - Expenses only for the business part of your home. Examples: Painting or repairs only in the area used for business.
- Deduct business portion - Expenses for keeping up and running your entire home. Examples: Insurance, utilities, and general repairs.
- Do not deduct personal portion - Expenses only for the parts of your home not used for business. Examples: Lawn care or painting a room not used for business.

Simplified Method

- Determine square footage used by farm - 300 sqft limit
- Multiply square footage by $5 for deduction amount

***Deduction may be carried forward, if farm has a Net Loss or if this deduction will cause a Net Loss

Question submitted earlier:

Guidance for when the farm uses part of a residence that is also rented out to a non-farm-involved tenant? Farm shares kitchen for incidental processing; has sole use of finished basement; sole use of bedroom, mudroom, and unfinished garage. Farm electric all comes from this house with no way to track separate usage. Then, how does the game change if the tenant leaves and I take his place sharing the house with the farm?

- Are the kitchen, basement, bedroom, mudroom and garage used exclusively and regularly by the farm?
- If the Actual Expenses cannot be pro-rated because of shared electric, then use the Simplified Method
- Remember cannot exceed 300 sqft for Simplified Method
- Recommend designating specific 300 sqft area that is used for the deduction
Question submitted earlier:

Construction supplies used to build a barn on our property have been reported on the Partnership tax return for the past 8 years. I’m wondering if this should have been reported on our personal return as business use of residence? If so, how do we correct it now?

- It depends....
- More on this question at the end, if time allows

Any additional business use of home questions?

We will discuss labor in more detail next....
More on Labor

**Employee**
- You direct & control the work performed
- You control the financial aspects of the worker's job
- Worker receives fringe benefits
- Expectation that job will continue indefinitely
- Services provided are key to the operation of the business
- Do not have to meet all of these requirements - seasonal workers, etc.

**Contractor**
- Worker decides when and how work if performed
- Worker controls financial aspects of the job
- There is a written contract outlining the services and pay
- Job is short-term or is only for a specific project
- Services are incidental to the operation of the business

More on Labor

- Classifying an employee as an independent contractor with no reasonable cause for doing so makes employers liable for employment taxes
- Failure to pay employment taxes on a quarterly basis can result in penalties and interest
- Audit regarding employment taxes can often be more intense than income tax audits
More on Labor

Employee
- Process payroll on a scheduled basis
- Withhold employment taxes - employee portion and employer portion
- Submit quarterly reports and pay withholding taxes
- Issue a W-2 by January 31 for work performed in the previous year

Contractor
- Business pays the contractor when a bill/invoice is received
- Retain paid invoice, cancelled check, and contract for business records
- No withholding or reports
- Issue a 1099-NEC (use to be 1099-MISC) by January 31 for payments over $600 made in previous year

Question submitted earlier:

How to calculate tax withholding on seasonal, part-time employees?
- Does the position fall within the parameters of employee (vs contractor)?
- Seasonal employees are treated the same as year-round employees
- Seasonal employers are only required to file withholding reports and pay taxes for the quarters they have employees
- Part-time employees are treated the same as full-time employees
- Actual tax calculation involves: withholding status, payment schedule, pay bracket, etc. for federal, state and possibly city withholding
Any additional labor questions?

33  Total expenses. Add lines 10 through 32f. If line 32f is negative, see instructions  

34  Net farm profit or (loss). Subtract line 33 from line 9  

If a profit, stop here and see instructions for where to report. If a loss, complete lines 35 and 36.

35  Reserved for future use.

36  Check the box that describes your investment in this activity and see instructions for where to report your loss:

a  [ ] All investment is at risk.  
b  [ ] Some investment is not at risk.
Profit or Loss Explanation

33. Total expenses...
34. Gross Income - Total Expenses = Profit or Loss. IRS safe harbor “rule”: a business should show a profit 3 out of 5 years or it could be classified as a hobby.
   The amount on line 34 is copied to the:
   - Form 1040 for Sole-Proprietor or Qualifying Joint Venture
   - Form 1065 for Partnership, which flows to the K-1 for each partner
   - Form 1120-S for an S-Corp, which flows to the K-1 for each partner
   - Form 1120 for a Corporation - taxes paid by corporation, 1099-DIV may be issued and shareholders pay taxes on the dividend amount

35. Reserve for future use...
36. Only money you are labile for is at-risk

Any additional Schedule F questions?
Typical Types of Taxes Paid by Farmers

Sales Tax

Self-employment Tax

Income Tax

Sales Tax

- Collected on TOTAL RETAIL sales - end customer is charged sales tax.
- Sales tax is collected by you for the government in the location the sale is made - it is not part of your farm revenue.
- Register for Sales Tax Number with the state Dept. of Revenue for each state where you have retail sales - may need MO and KS.
- Sales tax is collected for: state, county, city and special tax districts.
- Each entity has their own sales tax rate - they are added together.
Sales Tax

- All sales taxes are reported and paid to the state (in which the sale was made), who distributes the accurate portions to each county, city and special tax district.
- Report and pay to the government each payment period - varies based on annual sales amount.
- Farmer must register with the state to receive a Sales Tax Number ONLY for Value-added or resale
- Missouri exemption for farm products sold at farmer’s markets, if farm annual sales are $25,000 or less - no sales tax collection is required

Sales Tax Collected for Multiple Governments

4.225% Missouri  
1.250% Jackson Co  
3.250% KCMO  
0.125% Zoo District  
1.000% Street Car District  
9.850% Sales Tax Total Rate collected at City Market
Sales Tax

- Add on to total purchase price - Target, Walgreens, TSC, etc.
  - $8.00 sale price
  - 9.850% Sales Tax Rate
  - $0.79 Sales Tax
  - Sales amount reported = $8.00
  - $8.79 amount paid

- Back out of total purchase price - easier with farmer’s market cash purchases
  - $8.00 amount paid/1.0985 = $7.28 sale price
  - $8.00 - $7.28 = $0.72 sales tax
  - Sales amount reported = $7.28

Note: Target receives $0.79 more for the item than the farmer’s market booth.

Question submitted earlier:

Should I get a sales tax-exempt number for purchases? What kind of items can I buy with my tax-exempt number? Sometimes I tell Tractor Supply I’m tax-exempt and they don’t ask me for my number at all. But if I go into Walmart for ingredients for my value-added product or packaging for my vegetables they ask me for my sales tax-exempt number and make me fill out paperwork. What’s the difference?

- Many different categories of sales tax exempt - farm tax exempt, retailer purchase for resale, manufacturer purchase for production, non-profit tax exempt status, etc.
- Each state has designated Farm Tax Exempt categories, so a sales tax-exempt number is not necessary. If you are a farmer who purchases items in these categories, you are not required to pay sales tax. Focus is on the item category, not the tax status of the purchaser. Mo Form 149 and KS Pub. 1520
- Value-added (as discussed earlier) is not farming. For sales tax is can fall under resale or manufacturer - both are required to have a sales tax number. Focus is on the tax status of the purchaser, not the items purchased. Additional paperwork is required to track the sales tax status of the purchaser.
- Same paperwork is required for produce, flowers, etc purchased for resale. Sales tax is not charged until the final sale to the END customer.
Any additional Sales Tax questions?

Withholding & Self-employment Tax

- Taxes paid by everyone who earns money through employment
- Withholding is calculated and collected by your employer throughout the year
- Year end Withholding totals are reported on the W-2
- Self-employment tax is calculated on your tax return for the previous calendar year
- Both can be paid to city, state and federal governments
- Same tax rate for both Withholding & Self-employment taxes - collected under different methods
### Withholding & Self-employment Tax

**Withholding** - includes Medicare, Social Security & Income Tax

<table>
<thead>
<tr>
<th>Employee</th>
<th>Employer</th>
</tr>
</thead>
<tbody>
<tr>
<td>► Medicare - employee pays half</td>
<td>► Medicare - employer pays half</td>
</tr>
<tr>
<td>► Social Security - employee pays half</td>
<td>► Social Security - employer pays half</td>
</tr>
<tr>
<td>► Federal Income Tax - employee chooses rate withheld</td>
<td>► Also pays federal and state Unemployment Tax based on the company rates</td>
</tr>
<tr>
<td>► State Income Tax - employee chooses rate withheld</td>
<td></td>
</tr>
<tr>
<td>► KCMO Earnings Tax - 1% for anyone living or working in KCMO</td>
<td></td>
</tr>
</tbody>
</table>

**Self-employment** - only includes Medicare & Social Security

- Self-employment Tax must be paid if $400 or more Net Profit
- Self-employment Tax - both the employee and employer portions of Medicare and Social Security calculated on Net Profit
- Are allowed to deduct one-half of Self-employment Tax from your Adjusted Gross Income - more details discussed next
- If the farm Breaks-even or has a Net Loss, you do not pay into Social Security. A lower tax bill now may result in financially lean retirement years.
- Unemployment taxes are not paid
Withholding & Self-employment Tax

S-Corp Officers

- Receive a W-2 from the S-corp based on their “reasonable salary”
- Withholding is calculated on the W-2 as for any employee - Medicare, Social Security, federal income tax, state, income tax, city income tax
- Receive a K-1 from the S-corp based on their percentage of the Net Profit or Net Loss
- Amounts on the K-1 flow through to the individual 1040 tax return where income tax is calculated -
- S-Corp Officers do not pay Self-employment tax

S-corp Officers Example

If the S-Corp farm has $50,000 in earning, you can have that income paid out as $30,000 in salary and $20,000 in Net Profit. You’ll pay Medicare and Social Security taxes (S-corp pays half and Officer pays half) on just $30,000 instead of the whole $50,000. The remaining $20,000 of your income is only subject to income tax.

Things to consider...

The portion you choose for salary must be “reasonable” for the position held in the S-corp.

The S-corp must be profitable enough to have cash on hand to pay the salary every year.

You will be paying in less into Social Security, thus potentially reducing your retirement budget.
Any additional Withholding & Self-employed Tax questions?

Income Tax
Federal Return

- Farm Net Profit or Net Loss is combined with ALL OTHER sources of income to find TOTAL INCOME amount
- Any adjustments are applied and half of Self-employment tax amount is subtracted to find the ADJUSTED GROSS INCOME amount
- Deductions are subtracted from ADJUSTED GROSS INCOME to find TAXABLE INCOME amount
- Tax Rate is based on TAXABLE INCOME amount applied to the federal and state tax tables to calculate the TAX amount
- Tax Credits are subtracted and Self-employment tax is added to the TAX amount to find the TOTAL TAX
- Any previously made tax payments and additional credits are subtracted from TOTAL TAX to find PAYMENT DUE amount
Income Tax

- State tax calculations are similar to those on the federal return.
- Missouri and Kansas have reciprocal tax agreements, so you only need to report income and file a state return in the state you reside - different than Sales Tax.
- Kansas City has a 1% Earnings Tax on any Net Profits made while making sales inside the city limits or the Net Profits of any business located inside the city limits.

Estimated Tax Payments

- Only paid for Income Tax.
- Government requires that taxes are paid as income is received.
- Can assess penalties for not paying timely throughout the year.
- Estimated Tax payments have four due dates during the year.
- Payments can be made to the IRS and/or the state, as determined by the tax payment amounts.
Any additional Income Tax questions?

Other Questions or Discussion Topics?
Question submitted earlier:

1. Best practices for small beginning producers regarding reporting requirements?
2. What are your top 3 recommendations for young farmers as they navigate taxes?
3. Long term tax strategies for moving from old enterprises to new ones.
4. I’m interested in getting connected with a tax advisor who can help us make the best decisions regarding tax breaks and benefits for our brand new farm. We are just moving to a new property in KS as a multigenerational family ‘farm’ with different business and residences on the site.

- Establish a relationship with a tax preparer you trust. Meet with them to discuss your operation, business experience, goals an what information they will need for your taxes
- Keep up-to-date and ACCURATE records. If needed, hire someone to complete this task or find some training on a bookkeeping software. You won’t know if the farm is profitable (and worth your time) without accurate financial records
- BEFORE any significant financial decision - purchase, sale, investment, etc. - meet with your tax preparer. They can help you to ensure you to not have any surprises at tax time. Many experienced preparers can also recognize when it is good to recommend the services of a lawyer.

Question submitted earlier:

- Excellent choice to seek out a tax advisor! Once you find one you like, meet with them to discuss your operation, business goals and taxes.
- BEFORE any significant financial decision - purchase, sale, investment, etc. - meet with your tax preparer. They can help you to ensure you to not have any surprises at tax time. Many experienced preparers can also recognize when it is good to recommend the services of a lawyer.
Question submitted earlier:

- Establish a relationship with a tax preparer you trust. Meet with them to discuss your operation, business experience and goals.
- Keep up-to-date and ACCURATE records. If needed, hire someone to complete this task or find some training on a bookkeeping software. You won’t know if the farm is profitable (and worth your time) without accurate financial records.
- BEFORE any significant financial decision - purchase, sale, investment, etc. - meet with your tax preparer. They can help you to ensure you to not have any surprises at tax time. Many experienced preparers can also recognize when it is good to recommend the services of a lawyer.

Question submitted earlier:

Construction supplies used to build a barn on our property have been reported on the Partnership tax return for the past 8 years. I’m wondering if this should have been reported on our personal return as business use of residence? If so, how do we correct it now?

- Did the partnership pay for the construction or did you personally pay for the construction?
- What was the cost of the barn? Will the depreciation deduction exceed the Business Use of Home Simplified Method limitation of 300 sqft x $5 = $1500?
- Does the Partnership consists of a married couple who jointly own the property where the barn is located?
- It might pose a difficulty when the property/barn are sold. There would need to be a separate assessed value for the barn to determine capital gains and depreciation recapture.
- Option to amend the 8 years of tax returns to remove depreciation and replace with rental expense paid to the landowners or Business Use of Home.
- If the Partnership is an LLC, this might be a good topic to discuss with a lawyer to ensure the barn is protected under the LLC.
Thank you!

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