

TAX MANAGEMENT TIPS FOR FARMERS

L.R. Borton and J. Jones
Michigan State University

TelFarm

2025 - Tax Planning

1. The basic management guideline is to avoid wide fluctuations in taxable income because a relatively uniform income from year-to-year results in the lowest income tax and largest Farmland Preservation Credits over time. This also may apply to the Homestead Property Tax credit, if eligible.
 - a. The standard deduction is \$15,750 single, \$31,500 married filing jointly, \$23,625 head of household and extra for those 65 or older. The federal personal exemptions are now ZERO.
 - b. If total income is over \$137,000 married (\$88,100 single), the Alternative Minimum Tax (AMT) may apply and must be calculated to see if it increases your income taxes.
 - c. Qualified farmers (2/3 of gross income from farming in 2024 or 2025) do not have to pay estimated taxes if they file *and* pay all of the taxes due by March 1, 2026; or, pay estimated tax by January 15, 2026.
2. Tax rates and adjustments to income:
 - a. The 10% bracket on taxable income increased to \$11,925 for single and \$23,850 for married filing jointly. The top of the 12% bracket for married (\$96,950) is double that of singles (\$48,475). The higher brackets are 22%, 24%, 32%, 35%, and 37%.
 - b. For capital assets sold and installment payments received, capital gains rates for sale of long-term capital assets held over 12 months (over 24 months for breeding cattle and horses) are 0% if taxable income falls below \$48,350 single or \$99,700 married, filing jointly. Then it's 15% until taxable income reaches \$533,400 single and \$600,050 for married, filing jointly. The 20% long term capital gain rate applies to taxable income above that. Capital gains rates on collectibles remains at 28%.
 - c. The 3.8% net investment income (NII) tax applies to individuals, estates and trusts with modified adjusted gross income (MAGI) above \$250,000 for married filing jointly, \$200,000 for singles and \$15,650 for estates and trusts. NII includes gross income from interest, dividends, capital gains, rental and royalty income, nonqualified annuities, income from businesses involved in trading of financial instruments or commodities plus passive activity income. NII does not include wages, unemployment income, trade or business income, social security benefits, alimony, tax exempt interest, self-employment income and distributions from most retirement plans.
 - d. The sale of a principal residence is tax free on up to \$500,000 of gain for married filing jointly (\$250,000 single) if occupied by owner for two of last five years. Some exceptions may occur to the two of five years' rule and any use for other than a principal residence may reduce the non-taxable portion. The combination of a sale of a principal residence with a like-kind exchange of real estate used in a trade or business may allow some planning opportunities.
 - e. Penalty free IRA distributions may be taken to pay for qualified higher education expenses and certain expenses for a first-time homebuyer.
 - f. The section 179 (direct expense) deduction for capital purchases is \$2,500,000 in 2025, with the phase out beginning at \$4,000,000 of qualified property placed in service.
 - g. The income averaging provision for farm income (Schedule J) allows negative taxable income to be used from the three base years. Higher income years may use bracket amounts with lower rates leftover from the three previous years to reduce the tax due. The law coordinates AMT with farm income averaging so that averaging does not increase AMT.
 - h. For 2025 a 2-year net operating loss carry-back for farm losses is available and must be taken unless electing out of it. Can be carried forward indefinitely. The rule that a loss is limited to only reduce 80% of taxable income has returned. Consider offsetting current losses by converting regular IRAs to Roth IRAs.
 - i. Trade-Ins: When an asset that is personal property is traded-in, it must be treated as a sale. The purchased item is set up on a new depreciation schedule and includes the value of the traded-in item. This may result in lower SE taxes

compared to the previous like-kind exchange. Like-kind exchanges are still permitted for real property like land and attached property.

- j. The self-employed health insurance deduction is 100% on Form 1040 as an adjustment which still makes it subject to self-employment tax. It is limited to the net earned income from the business under which it has been setup. But it can't be combined with other businesses of the taxpayer.
 - k. Child tax credit is up to \$2,200 for children under 17 as of December 31. Phaseout begins at \$400,000 for married, filing jointly, or \$200,000 for others. A family tax \$500 credit is available for any dependent that does not qualify for the child tax credit.
 - l. The Domestic Production Activities Deduction (DPAD) is GONE. There is a DPAD, similar to the old one, that cooperatives may use and pass to its members.
 - m. The phase-out of personal exemptions is GONE since the exemption is zero.
 - n. The overall limitation of itemized deductions is GONE. Many more taxpayers and most farmers use the standard deduction anyway.
 - o. Qualified Business Income Deduction (QBI). A 20% deduction of net profit from a sole proprietorship, partnership or S corporation (pass through of profits to taxpayers) is available for businesses to go along with the constant 21% tax rate on C corporations. There are maximum limits to this deduction to taxable income but most farms that pass through their profits should qualify. LLCs taxed as sole proprietorships, partnerships or S corporations are eligible for the QBI deduction. LLCs taxed as C corporations are not eligible since their tax rate is 21%.
3. Depending on your tax situation, you may wish to reduce or increase net income for 2025. Following are some of the best income eveners:
- a. Buy or delay purchase of supplies such as fertilizer, seed, farm supplies, small tools, and repairs (tax shelters can only deduct items when used). Note: prepaid expenses should normally not exceed 50% of your total other Schedule F expenses for the year for which economic performance has occurred. The repair and capitalization regulations changed little for cash accounting farmers that prepay supplies.
 - b. Pay in 2025 or delay payment to 2026 on real estate taxes and other annual bills. (Insurance premiums, real estate rental for 2026 and interest cannot be paid more than 12 months in advance to obtain an earlier tax deduction, but 2025 expenses of insurance, rentals and interest can be deferred to 2026 if income is low this year).
 - c. Watch the timing of sales of livestock and crops ready for market near year-end. Perhaps they can be held for sale next year at little cost or sold earlier to even out taxable income. CCC loans can count either as borrowed funds or as income if the appropriate forms are filed.
 - d. For farmers using cash method accounting, crop insurance or disaster payments may be reported in the year received or may be postponed one year under qualifying circumstances.
 - e. The gain may be postponed one year for livestock sold in excess of normal business operations if it's due to a weather-related lack of feed or water. For dairy, draft or breeding livestock sold in excess of normal practices, gain may be deferred if replacement livestock are purchased within two years of the end of the tax year of the excess sale. This may become four years or more under some conditions.
 - f. Some expenses are deductible as current year business expenses even though not made every year. These include minor repairs on improvements and machinery, painting of buildings, purchase of small tools and supplies, and within limitations, cost of approved soil and water conservation expenses. Get these jobs done and paid for before year-end if you wish to reduce net income. Under the repair regulations, a farmer without an Applicable Financial Statement (most farmers do not have one) can deduct all items purchased up to \$2,500 per item. The amount can be reduced below \$2,500, if desired. This election is made on the tax return.
 - g. Where capital purchases have been made, or can be made, study the depreciation alternatives carefully. The direct expense deduction of up to \$2,500,000 can be taken on current year capital purchases. Its use, however, cannot reduce your taxable income from farming (plus other earned income) below zero. Taxable income from farming includes net farm profit plus gains on the sale of business assets such as breeding livestock. There are four choices for depreciation on used machinery: Modified Accelerated Cost Recovery System (MACRS) 7-year (GDS) 200% declining balance, MACRS 7-year (GDS) 150% declining balance, MACRS 7-year (GDS) straight

line; and the Alternative Depreciation System (ADS), which is 10-year straight line. (Note that new machinery and equipment is 5 year property except for new grain bins and new fences which are still 7 year). Also, 200% declining balance may be used for 3, 5, 7 or 10 year farm property. For the first year of depreciation the half-year convention is used (1/2 year's depreciation), unless 40% or more of your capital purchases after direct expensing are made during the last 3 months of the year. In that case, the mid-quarter convention is used (87.5% of a year's depreciation for purchases made during the first 3 months, 62.5% for purchases in second quarter, 37.5% for third quarter, and 12.5% in final quarter).

- h. The additional first year depreciation or bonus depreciation is permanently 100% for purchases after January 19, 2025. It is required for most new OR used, farm depreciable property. For 2025 an election for 40% bonus is available. Taxpayers may elect out of bonus by class of property (3, 5, 7, 10, 15 or 20-year property). It is taken after direct expensing and before normal depreciation. Even if required to use ADS, a special rule enables bonus depreciation to be taken on the cost of fruits, vines and nuts in the year planted.
- i. Pay your children wages for work actually performed for the farm. Be reasonable and age appropriate for work and wages. If the child is under 18 and works for a parent's trade or business, their wages may be subject to income tax withholding, but are exempt from Social Security and Medicare taxes.
- j. For Michigan income tax, an individual who is eligible to be claimed as a dependent on someone else's return and has an adjusted gross income of \$1,500 or less is entitled to a refund of all Michigan tax withheld. The Michigan income tax rate for 2025 is 4.25%. The exemption amount for Michigan is \$5,800 for 2025.
- k. Frequently unrecorded and forgotten expenses include:
 - i. Educational expenses that maintain or improve your skills, such as magazine subscriptions, books, fees at extension or other agricultural organization meetings.
 - ii. Travel expenses connected with your business, particularly if it includes meals and lodging.
 - iii. Business meals are 50% deductible in 2025.

4. Self-Employment Tax: Most taxpayers and many farmers pay more in SE tax than federal income tax.

- a. Social Security and hospital insurance rates for the self-employed are 12.4% and 2.9% for a total of 15.3% on 0.9235 of net farm profit up to \$176,100 for 2025. In addition, the 2.9% Medicare tax continues on income over \$176,100. A 0.9% additional Medicare tax applies to wages and SE income over \$200,000 for single filers and \$250,000 for married filing jointly.
- b. To earn one quarter of work credit of coverage in 2025, \$1,810 of earnings are required. 50% of the Self Employment tax will be deducted as an adjustment to income on the federal form.
- c. In 2025, farmers who have less than \$10,860 gross farm income may elect to pay SE tax on 2/3 of their gross farm income or if gross farm income is greater than \$10,860 may elect to pay SE tax on \$7,240 even if they would not otherwise owe SE tax. This allows a taxpayer to earn four quarters or work credits each year towards social security and disability eligibility. The amounts are indexed to increase with inflation. Much or all of the SE tax paid may be returned through the Earned Income Credit.
- d. Conservation Reserve Program payments for those receiving social security or certain disability payments are not included in self-employment income and were not subject to SE tax beginning in 2008. For those receiving social security payments prior to their full retirement age, the CRP payments will not count as earned income for the \$23,400 annual earned income limit in 2025. The Morehouse decision from the 8th Circuit Court does not apply to Michigan. It said that non-farmers are not subject to SE tax on CRP payments. The IRS disagrees and still contends that CRP payments are subject to SE tax.

Other Tax Planning Ideas

- 1. Maintain a good set of records to ensure that all expenses are taken. Small cash purchases are easily forgotten. A good system is essential for end-of-year tax planning and working with credit agencies.

2. A new, permanent \$1,000 single deduction (\$2,000 MFJ) for cash donations to charitable organizations is for those who do not itemize (starts in 2026). A new, senior deduction of \$6,000 for each person over 65 begins phaseout at \$75,000 single (\$150,000 MFJ). Phases out at 6% for each \$6,000 deduction and is available 2025 through 2028 (for both itemized deductions or standard deduction).
3. Plan your personal deductions to use bunching. Many medical expenses and contributions formerly spread over 2 years can be paid in 1 year and itemized as deductions. In the next year, the standard deduction may be taken. Itemized deductions include medical expenses in excess of 7.5% of AGI, no personal interest is deductible, moving expenses are not deductible except for military with orders. Miscellaneous itemized deductions are permanently not allowed.
4. Investigate a Self-employed Retirement Plan. A Simplified Employee Plan (SEP IRA with a limit of \$70,000) requires that certain employees also be covered. A SIMPLE plan is best for small employers to encourage employee retirement savings without costly administration (up to \$16,500 plus \$3,500 for those age 50 or older). Another alternative is an Individual Retirement Account (IRA). Employees do not have to be covered if a self-employed person utilizes an IRA; however, the maximum contribution is \$7,000 per year in 2025, with an additional \$7,000 in spousal IRA (plus an additional \$1,000 for each one age 50 or over). A traditional IRA deduction cannot be used if the contributor is eligible to participate in another retirement plan and modified AGI exceeds \$146,000 for a married filing joint taxpayer, or \$89,000 for a single taxpayer (reduced contributions can be made for AGI down to \$126,000 and \$79,000, respectively). A Roth IRA contribution can be made with after tax dollars, but proper distributions should be tax exempt. Phase-outs for Roths are \$236,000 to \$246,000 for joint returns and \$150,000 to \$165,000 for single filers. Some taxpayers contribute to a traditional IRA with after tax dollars and then transfer it to a Roth IRA. If wanting to do this, check ALL the rules closely.
5. Where income is low or negative, consider the transfer of traditional IRA or 401(k) retirement balances to a Roth IRA and increase income this year and take advantage of future non-taxable income. Don't expect lower tax rates in the future.
6. Your farm business is a built-in deferred compensation and tax loss program. Investments and current expenses are made that improve the value of the business property which can be sold at a later date, frequently at capital gains rates. Establishing a fruit orchard or increasing the size of a breeding livestock herd fits this situation. Crops in this category are timber, fruit trees, and Christmas trees as well as the build-up in year-end inventories.
7. Use installment sales of capital items to spread income over a number of years, but check your expected tax bracket and remember that all depreciation recapture occurs in the year of sale even if no money is received until the following year. Before scheduling a sale of the farm business due to retirement or bankruptcy, check into the income and self-employment taxes. Gains from the sale of property may result in significant tax consequences without careful planning.
8. If approaching retirement, plan for more of your income from rent, dividends, interest, and pensions rather than earned income so that income will not be taxed as self-employment income for Social Security or reduce Social Security benefits. Earned income level that will decrease Social Security benefits for 2025 is at \$23,400 per year for those under full retirement age. The decrease is \$1 for every \$2 of excess earnings. In the year that full retirement age is reached, the decrease is \$1 for every \$3 of earnings in excess of \$62,160 per year (\$5,180 per month) until the month that age is attained. There is no limit on earnings when full retirement age is attained. That is age 66 years for those born from 1943 to 1954, but Social Security taxes are still paid on earned income. For each birth year after 1954, two months are added to full retirement age up to the 1960 birth year. Those born in 1960 or after may be eligible for social security at 62 but won't reach full retirement age until turning 67.
9. Be sure to deduct as large a portion of business-personal expenses as is justified in your situation. Considerably more than 50% of the electricity and phone costs may be considered business. Also, choose the method for auto deductions which is best for you. The standard mileage rate for 2025 business mileage is 70.0 cents per mile. Mileage for charitable purposes can be itemized at 14 cents per mile, for medical at 21.0 cents per mile. Few taxpayers, except military, qualify for moving expense mileage.

10. Be aware of the Alternative Minimum Tax in tax planning. It is a completely separate method to calculate income tax due. Alternative Minimum Taxable Income (AMTI) includes tax preference items such as tax-free interest. There is an \$137,000 exemption for those filing joint returns (\$88,100 single). The threshold levels for phaseout and reduction of the AMT exemption amount is \$1,252,700-\$1,800,700 for MFJ and \$626,350-\$978,750 for single. It is paid to the degree the tax exceeds your regular tax.
11. The lower long-term capital gain rate is 0% and applies for long term capital gain below taxable income of \$48,350 (\$96,700 for MFJ). Where taxable income is above those levels, long term capital gain rate becomes 15%. Portions of gain often are taxed at both rates because the lower rate applies until the higher taxable income bracket is reached, then the higher rate applies. The 20% rate applies when taxable income is above \$533,400 single (or \$600,050 MFJ).
12. The Kiddie Tax applies to dependent children who are either up to 18 years or full-time students under 24 years old. Unearned income (not wages or scholarships) over \$2,700 (for 2025) will be taxed at the parents' rate.
13. Credits may reduce taxes. Refundable credits can be received even if no taxes are owed. Non-refundable credits can be used only if income taxes are owed.
 - a. Earned income Credit (refundable) – Maximum of \$8,046 with 3 children, AGI phase-out completed by \$68,675 for married, filing jointly. Maximum of \$7,152 with 2 children, \$4,238 with one child, and \$649 with no children. Phase-outs are lower for other than married, filing jointly. Michigan also has an EIC which is 30% of the federal EIC.
 - b. Education Credits – The American Opportunity Credit is a maximum of \$2,500 per student in their first four years of college. AGI phase-out of \$160,000-\$180,000 married, filing jointly and \$80,000-\$90,000 for others. Lifetime learning credit of 20% of qualified, educational expenses up to \$10,000 (maximum of \$2,000 credit) but phases out at the same limits.
14. For tax years required to be filed in 2025, the penalty for failure to file a partnership or S corporation return increased to \$255 per partner or shareholder per month up to a maximum of 12 months.
15. Farm businesses are still required to issue Form 1099-MISC or Form 1099-NEC for \$600 or more payments for rents and services except for payments to corporations. An LLC is probably not a corporation and payments for renting land or custom machine work still requires a form. Give a Form W-9 to the landowner or operator to obtain the necessary information. Note that even veterinary services that are corporations must be given a form if \$600 or more is paid for services since they are partly medical services. Penalties can apply for failing to file an information return with the IRS and an equal penalty for not giving one to the recipient. This might even occur when a retired member of the family rents land to an operating entity. The 2025 Form 1099-NEC is used to report non-employee compensation or services to a professional or person who is not your employee.
16. Properly donating commodities to charitable organizations may reduce income compared to selling the commodity and then donating cash. For example, donate grain the year after it is produced and all the costs of production were deducted the prior year for cash method of accounting. There is no charitable deduction but the reduced income will reduce self-employment tax and may save income tax.
17. The annual exclusion for gifts is \$19,000 per individual while the gift tax applicable exclusion amount is \$13,990,000. If properly elected, the amount of the exclusion that is unused by the estate of the first spouse to die can be used by the surviving spouse. Realize that more may be given, but some paperwork may be required or taxes might then apply.
18. If unsolicited emails are received from the IRS asking for information or money, then it's probably a scam. Any attachments will probably try to put a virus on your computer. Beware! Do not open the email; just delete it. If someone calls claiming to be the IRS and wants money, don't send money because it is a scam.

19. The Michigan income tax rate for 2025 remains at 4.25% and the personal exemption is \$5,800. The home heating credit and homestead credit are based on Household Resources while the Farmland Open Space and Preservation credit is still based on Household Income.
20. In tax years beginning after July 4, 2025, taxpayers can elect to pay tax on the gain from the sale or exchange of qualified farmland property in installments over four years.
21. The Affordable Care Act (Obamacare) has an individual shared responsibility provision which requires you and each member of your family to either:
 - a. Have minimum essential coverage, or
 - b. Have an exemption from the responsibility to have minimum essential coverage, or
 - c. Make a shared responsibility payment

The individual penalty for not maintaining minimum essential coverage was eliminated in 2019. Note that the Premium Tax Credit rules have changed so check with your insurance carrier.

Agricultural or Horticultural Cooperatives

While the Domestic Production Activities Deduction is gone, a specified cooperative provides a deduction for qualified production activities income (QPAI). It is calculated by the cooperative by taking 9% of the lesser of the cooperatives QPAI or taxable income. It is limited to 50% of the wages paid by the cooperative. (sounds very similar to the DPAD passed through to members by the cooperative).

In addition, the patronage dividends and per unit retains paid in money (we used to call this sales to the cooperative) count as income used in computing a farm's Qualified Business Income (QBI). However, the QBI deduction gets reduced by the lesser of 9% of the QBI from the payments received from the cooperative OR 50% of the wages paid by the farm for labor allocated to the products delivered to the cooperative for those payments received.