

Taxes for Agricultural Enterprises

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Section 3: Farm Income

Section 3: Farm Income

- Sales of livestock and other items purchased for resale
- Sales of livestock, produce, grains and other products
- Commodity Credit Corporation (CCC) loans
- Agricultural program payments
- Conservation Reserve Program (CRP) payments
- Other income

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This section provides information explaining income that can and should be reported on the Form 1040 Schedule F including sales of livestock and other items purchased for resale, sales of produce, grain and other products raised, CCC loans, Agricultural program payments, CRP payments, and other income.

Form 1040 Schedule F Income

Part I Farm Income—Cash Method. Complete Parts I and II (Accrual method. Complete Parts II and III, and Part I, line 11.)
 Do not include sales of livestock held for draft, breeding, sport, or dairy purposes; report these sales on Form 4797.

1	Sales of livestock and other items you bought for resale				
2	Cost or other basis of livestock and other items reported on line 1				
3	Subtract line 2 from line 1				
4	Sales of livestock, produce, grains, and other products you raised				
5a	Cooperative distributions (Form(s) 1099-PATR)	5a		5b Taxable amount	5b
6a	Agricultural program payments (see page F-2)	6a		6b Taxable amount	6b
7	Commodity Credit Corporation (CCC) loans (see page F-3):				
a	CCC loans reported under election			7a	
b	CCC loans forfeited	7b		7c Taxable amount	7c
8	Crop insurance proceeds and Federal crop disaster payments (see page F-3):				
a	Amount received in 2005	8a		8b Taxable amount	8b
c	If election to defer to 2006 is attached, check here <input type="checkbox"/>			8d Amount deferred from 2004	8d
9	Custom hire (machine work) income				9
10	Other income, including Federal and state gasoline or fuel tax credit or refund (see page F-3)				10
11	Gross income. Add amounts in the right column for lines 3 through 10. If you use the accrual method, enter the amount from Part III, line 51				11

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Income earned from agricultural businesses is reported on Schedule F. Here is how the farm income part of Form 1040 Schedule F looked for the 2005 tax year.

Income reported on Schedule F does not include gains or losses from sales or other distributions of farm assets including land, depreciable farm equipment, buildings and structures, and livestock held for draft, breeding, sport, or dairy purposes.

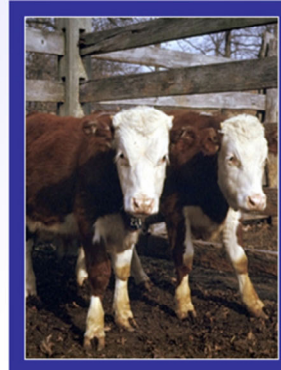
Farm Income Categories

Part I Farm Income—Cash Method. Complete Parts I and II (Accrual method. Complete Parts II)
Do not include sales of livestock held for draft, breeding, sport, or dairy purposes; report:

1	Sales of livestock and other items you bought for resale	1	
2	Cost or other basis of livestock and other items reported on line 1	2	
3	Subtract line 2 from line 1		
4	Sales of livestock, produce, grains, and other products you raised		
5a	Cooperative distributions (Form(s) 1099-PATR)	5a	5b Taxable amount
6a	Agricultural program payments (see page F-2)	6a	6b Taxable amount
7	Commodity Credit Corporation		
a	CCC loans reported under		
b	CCC loans forfeited		
8	Crop insurance proceeds		
a	Amount received in 2005		
c	If election to defer to 2006		
9	Custom hire (machine work)		
10	Other income, including Federal		

Sales of livestock and other items purchased for resale

- Sales of farm products purchased for resale
- Profit or loss is the difference between the basis in the item, usually the cost, and any payments received
- Basis may have been carried forward from a previous year



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Income reported on Schedule F includes amounts received from cultivating, operating, or managing a farm for gain or profit, either as owner or tenant as well as income from operating a stock, dairy, poultry, fish, fruit, or truck farm. It also includes income from the sale of crop shares if the landowner materially participated in producing the crop is also included. This highlighted category in the Schedule F will show us more: (read bullets).

Farm Income Categories

Sales of livestock, produce, grains and other products raised

- Sales of all raised products



Part I Farm Income—Cash Method. Complete Parts I and II (Accrual method. Complete Parts II Do not include sales of livestock held for draft, breeding, sport, or dairy purposes; report

1	Sales of livestock and other items you bought for resale		1	
2	Cost or other basis of livestock and other items reported on line 1		2	
3	Subtract line 2 from line 1			
4	Sales of livestock, produce, grains, and other products you raised			
5a	Cooperative distributions (Form(s) 1099-PATR)	5a		5b Taxable amount
6a	Agricultural program payments (see page F-2)	6a		6b Taxable amount
7	Commodity Credit Corporation (CCC) loans (see page F-3):			
a	CCC loans reported under election			
b	CCC loans forfeited	7b		7c Taxable amount
8	Crop insurance proceeds and Federal crop disaster payments (see page F-3):			
a	Amount received in 2005	8a		8b Taxable amount
c	If election to defer to 2006 is attached, check here <input type="checkbox"/>			8d Amount deferred from 2004
9	Custom hire (machine work) income			
10	Other income, including Federal and state gasoline or fuel tax credit or refund (see page F-3)			

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This highlighted category in the Schedule F will show us more: (read bullets).

Hedging as Risk Management

- Hedging transactions entered into in normal course of business
- For risk management purposes
- As forward contracts, futures contracts, options
- Commodity is produced on the farm or directly affects the business
- Generally an ordinary gain or loss
- Reported on Schedule F



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Hedging transactions are transactions entered into in the normal course of business primarily to manage risk. Farmers, to protect themselves from the risk of unfavorable price fluctuations, may enter into commodity forward contracts, futures contracts, or options on futures contracts. If the contracts cover an amount of the commodity within the range of production, the transactions are generally considered hedging contracts. They can take place at any time the commodity is under production, is on hand for sale, or is reasonably expected to be on hand.

Hedging as Speculation

- Hedging transactions entered into which are not part of the ordinary business of farm
- Has specific record keeping requirements
- Reported on Form 1040



Farmers and ranchers may also buy and sell commodities as speculators. Hedging and speculation transactions must be reported separately on the income tax return. It may be helpful to have separate brokerage accounts for the two types of transactions. The identification must specify both the hedging transaction and the item, items, or aggregate risk that is being hedged. Although the identification of the hedging transaction must be made before the end of the day it was entered into, the hedged item, items, or risk must be identified within 35 days after entering into the transaction.

Hedging vs. Speculation

- Hedging Transactions
- Speculation Transactions



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From an income tax perspective, hedging transactions are defined in terms of reducing the risk of price fluctuations (or interest rate fluctuations) in the ordinary course of the taxpayer's business.

Gains and losses that do not qualify as hedges, but instead are speculation, and do not involve contracts primarily for sale to customers in the ordinary course of a trade or business, are treated as capital gains and losses.

Activity:
Farm Income or Not Farm Income

Part I Farm Income—Cash Method. Complete Parts I a
Do not include sales of livestock held for draft, bre

1	Sales of livestock and other items you bought for resale . . .	
2	Cost or other basis of livestock and other items reported on line 1 . . .	
3	Subtract line 2 from line 1 . . .	
4	Sales of livestock, produce, grains, and other products you raise . . .	
5a	Cooperative distributions (Form(s) 1099-PATR) . . .	5a
6a	Agricultural program payments (see page F-2) . . .	6a
7	Commodity Credit Corporation (CCC) loans (see page F-3):	
a	CCC loans reported under election . . .	
b	CCC loans forfeited . . .	7b
8	Crop insurance proceeds and Federal crop disaster payments:	
a	Amount received in 2005 . . .	8a
c	If election to defer to 2006 is attached, check here <input type="checkbox"/> . . .	
9	Custom hire (machine work) income . . .	
10	Other income, including Federal and state gasoline or fuel tax cred . . .	
11	Gross income. Add amounts in the right column for lines 3 thro, the amount from Part III, line 51 . . .	

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Lets see if we can decide whether a scenario needs to be reported as Farm income or as Non Farm income.

1. SALE OF CATTLE YOU RAISED – FARM INCOME
2. CASH RECEIVED FROM FARM MARKET SALES – FARM INCOME
3. CASH RECEIVED FROM DIGGING A NEIGHBOR'S FIELD USING YOUR WON FARM EQUIPMENT – FARM INCOME
4. MONEY RECEIVED FROM SALE OF PURCHASED EWES – NON FARM INCOME (contracts primarily for sale to customers NOT in the ordinary course of a trade or business, are treated as capital gains and losses and are not reported on Schedule F, but elsewhere on the 1040)
5. CROP INSURANCE PROCEEDS – FARM INCOME

Section 3: Summary

- Sales of livestock and other items purchased for resale
- Sales of livestock, produce, grains and other products
- Commodity Credit Corporation (CCC) loans
- Agricultural program payments
- Conservation Reserve Program (CRP) payments
- Other income



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Summary

- Income earned from agricultural businesses is reported on Schedule F. Income from farming includes amounts received from cultivating, operating, or managing a farm for gain or profit, either as owner or tenant
- Schedule F Income includes income from operating a stock, dairy, poultry, fish, fruit, or truck farm, sales of all raised products, sales of farm products purchased for resale, all agricultural program payments, including CRP payments, CCC loans, crop insurance proceeds, federal tax gas credit, hedging transactions and other Income
- Income reported on Schedule F does not include gains or losses from sales or other distributions of farm assets including land, depreciable farm equipment, buildings and structures, and livestock help for draft, breeding, sport, or dairy purposes
- Income tax law differentiates hedging from speculation