

Like any small business, farmers are liable for paying a variety of taxes. Variables such as your form of business, whether you own your land, have employees, sell non-food items, and where and how you sell your farm products all affect the taxes that you are responsible for. There are some farm exemptions from paying taxes. This fact sheet is intended to help you navigate the world of taxes, and your responsibilities and exemptions as a farmer and entrepreneur.

This fact sheet includes information on:

- Federal taxes - Schedule F and labor-related taxes.
- Washington State and local taxes - business and sales taxes.
- Washington State labor-related taxes.

This information is for general educational purposes only and is not intended to take the place of professional advice from lawyers and certified public accountants.



Federal Taxes

The Internal Revenue Service (IRS) website provides detailed information, including guidance publications for the following federal tax topics. Search [irs.gov](https://www.irs.gov), by publication number or tax name.

The form of business, such as sole proprietorship, LLC, S Corp, B Corp, etc., determines the taxes you will have to pay. Search for "Business Structures" at [irs.gov](https://www.irs.gov) to find out which records to keep and which returns you must file based on your type of business entity.

The "Farmers Tax Guide," Internal Revenue Service (IRS) Publication #225, online at [irs.gov](https://www.irs.gov), explains in detail how the federal tax laws apply to farming, and highlights annual administrative and tax law changes. Use this publication as a guide to figure your taxes and complete your farm tax return.

NOTE: The Tax Cuts and Jobs Act of 2017 included several changes that affect farmers and ranchers, including net operating losses, pass-through entities, accounting method changes, inventory, depreciation and personal casualty, and theft losses. Find details about the changes and more by searching for "What's new for farmers" in the IRS's Agricultural Tax Center at [irs.gov](https://www.irs.gov).



IRS Schedule F: Profit or Loss from Farming

Self-employed farmers report income and expenses from their farming business using IRS Form 1040 Schedule F. Schedule F is only for farmers who have their business incorporated as a sole proprietorship. Schedule F is to farmers what Schedule C is for other sole proprietors. If you are the sole member of a domestic LLC engaged in the business of farming, you may also file Schedule F.

The key to preparing an accurate tax return is to keep excellent records of your income, crops, livestock, other assets, and various expenses. Using accounting software can be very helpful. Farmers may receive income from many sources, but the most common source is the sale of livestock, produce, grains, and other products raised or bought for resale. Report the entire amount you receive, including money and the fair market value of any property or services.

Bartering is another income source for farmers. Bartering occurs when trading farm products or property for another farm's products or property, or someone else's labor or personal items. For example, if a farmer helps another farmer build a barn and receives a cow for the work, the recipient of the cow must report its fair market value as ordinary income. If the farmer uses this cow for business purposes, they may be able to claim depreciation over its useful life, as well as deduct the expenses incurred for the cow. However, if the bartered item is for personal and not business use, no depreciation or expenses would be deductible.

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The ordinary and necessary costs of operating a farm for profit are deductible business expenses. These include farm labor and depreciation.

If a farmer pays their child, or other dependent family member to do farm work and a true employer-employee relationship exists, reasonable wages or other compensation paid to the family member are deductible. The wages are included in the family member's income, and that person will have to file an income tax return. For details, refer to Filing Requirements for Dependents in IRS Publication 501, "Exemptions, Standard Deduction and Filing Information." These wages may also be subject to Social Security and Medicare taxes if the family member is age 18 or older.

Farmers can depreciate most types of tangible property such as buildings, machinery, equipment, vehicles, certain livestock, and furniture. The big exception is land; farms cannot deduct depreciation for land. Farmers can also depreciate certain intangible property, such as copyrights, patents, and computer software.

To be depreciable, the property must meet **all three** of these criteria:

1. Be property the farmer owns.
2. Be used in the farmer's business or income-producing activity.
3. Have a useful life that extends substantially beyond the year placed in service as defined by the IRS.

Some expenses paid during the tax year may be partly personal and partly business. Examples include gasoline, oil, fuel, water, rent, electricity, telephone, automobile upkeep, repairs, insurance, interest, and taxes. Farmers must allocate these expenses between their business and personal allocations. Generally, the personal part of these expenses is not deductible as a business expense.

For example, a farmer paid \$1,500 for electricity during the tax year. They used one-third of the electricity for personal purposes and two-thirds for farming. Under these circumstances, two-thirds of the electricity expense, or \$1,000, is deductible as a farm business expense. Be aware of the required documentation and record keeping for the business portion of the expense.

When an insured farm property is damaged, destroyed, or lost due to a sudden, unexpected, or unusual event, loss is then included with other business income and expenses to determine total taxes owed. You may have taxable losses or gains even if there is only partial damage. Deductible losses are incurred by many events, including vehicle accidents, fires, floods, freezing, lightning, tornadoes, terrorist attacks, and others. Please see the Fact Sheet on Insurance for related risk management information.

Find information about other deductible expenses and reporting requirements in the IRS Publication 225, "Farmer's Tax Guide" on the IRS website, [irs.gov](https://www.irs.gov).

Self-Employment Tax

You are considered self-employed by the IRS if any of the following apply:

- You carry on a trade or business as a sole proprietor or an independent contractor.
- You are a member of a partnership that carries on a trade or business.
- You are otherwise in business for yourself.

Federal self-employment tax (SE tax) is a Social Security and Medicare tax primarily for individuals who work for themselves. It is similar to the Social Security and Medicare taxes withheld from the pay of most wage earners. You must pay SE tax and file Schedule SE (Form 1040) if your net earnings from self-employment were \$400 or more. The SE tax is your contribution to Social Security and Medicare and is based on a percent of gross earnings. You must estimate your income taxes and make quarterly payments. Penalties apply for late and under payments.

Federal Payroll Taxes

If you have employees, you are required to pay both federal and state payroll taxes. (See below for state payroll taxes.) The federal payroll taxes are for Social Security and Medicare. Employees and employers share these taxes. Employers are required to deduct or "withhold" the employee share (one-half the total due) from wages/salaries, and pay the other half to the IRS.

Payroll taxes are required by law to be withheld from an employee's paycheck and it is the employer's responsibility to pay these taxes to the IRS.

Generally speaking, employers report payroll by calculating gross pay and various payroll deductions to arrive at net pay. While this seems simple enough to understand, calculating various payroll deductions requires that the person responsible for payroll be detail-oriented and work with extreme accuracy.

Payroll tax deductions include the following:

- Social Security tax withholding (6.2% up to the annual maximum)
- Medicare tax withholding (1.45%)
- Federal income tax withholding (based on withholding tables in IRS Publication 15 and built into accounting software)

Using accounting software or a payroll service can be very helpful in managing your payroll tax responsibilities.

Another great resource for understanding the administrative side of agriculture income, deductions and self-employment tax is ruraltax.org, hosted by Utah State University Cooperative Extension, members of the National Farm Income Tax Extension Committee.

Unemployment Insurance Taxes

You are also liable for federal unemployment tax. The Federal Unemployment Tax Act (FUTA), together with state unemployment systems, provides unemployment compensation to workers who have lost their jobs. Most employers pay both a federal and a state unemployment tax. FUTA is an employer only tax, meaning the employee is not responsible for any portion of this tax.

Washington State and Local Taxes

The Washington State Department of Revenue (DOR) is the source for information about all state taxes. The DOR publishes several key resources specifically to guide small, agricultural, and new businesses to help understand which state taxes apply to your farm business and how to plan for them. Search for these resources by name on the DOR website, dor.wa.gov or call 1-800-647-7706:

- “New Business Tax Basics” publication, and look for in-person workshops.
- “Agricultural Tax Guide” highlights the relevant taxes for different farm businesses.

- “Plan for and pay your taxes” tutorial video series that walks you through the steps.
- “Find taxes and rates” lists updated rate information for sales and other taxes.

Washington State does not have a corporate or personal income tax. However, the majority of Washington businesses are subject to one or more of the following three taxes:

1. Business and occupation tax (B&O)
2. Retail sales tax
3. Use tax.

Washington businesses may also be responsible for local property taxes. If a business has employees, it is responsible for state employer taxes and insurance premiums.

1. Business and Occupation (B&O) Tax

The state Business and Occupation (B&O) tax is based on your gross business income from activities. It is measured on the value of products, gross proceeds of sale, or gross income of the business. This means there are no deductions from the B&O tax for labor, materials, taxes, or other costs of doing business.

The B&O tax rate varies by classification. The DOR has several Business and Occupation tax tools on their website to help determine the right classification for your business. Look for information on Business and Occupation taxes and rates at dor.wa.gov. Once you know which classification your business fits into, you can find the rate that corresponds to your classification on the list of B&O tax rates.

The B&O tax is reported and paid to DOR on the excise tax return by electronic filing, or on a paper return in some cases. Register with DOR to set up an account using your Universal Business Identification (UBI) number. (See the “Licensing Fact Sheet” for information about setting up a business and obtaining a UBI number.) Once you are registered, DOR will send you information about filing taxes. You may be required to file monthly, quarterly, or annually. Note the payment dates included in the information from DOR.

B & O Deductions, Credits, and Exemptions

Farmers who wholesale products that they have grown or raised on their farm qualify for a B&O tax exemption and are not required to report income from this activity to the Department of Revenue.

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Fresh fruit and vegetable manufacturers do not owe B&O tax on certain manufacturing and selling activities through June 30, 2025. Manufacturing activities include canning, preserving, freezing, processing, or dehydrating fresh fruits or vegetables.

There are also B&O deductions available for dairy manufacturers. An advisory on how to file dairy manufacturing deductions is available by searching dor.wa.gov for the term "Dairy Product Manufacturers."

B&O tax credits may be issued by the Legislature for special purposes such as rural county credit for new employees, small business, or hiring unemployed veterans. Check with the DOR for details on allowable credits.

All businesses claiming B&O deductions are required to file an Annual Tax Incentive Survey online by April 30 of the year that follows the year the exemption is claimed. For example, if you claim B&O tax deductions in 2020, you must file an annual survey by April 30, 2021 by logging in to "My Account" on the DOR website and clicking through "Credits and Tax Incentives."

Many municipalities levy an additional B&O tax on all business conducted within their jurisdiction. Check with the local taxing authority such as the city finance department or treasurer. A listing of contacts for tax and licensing requirements for cities and counties in Washington is available from the DOR Business Licensing Service webpage, bls.dor.wa.gov/citycounty.

2. Retail Sales Tax

Washington's principal revenue source is retail sales tax. Businesses making retail sales in Washington collect sales tax from their customers. Generally, a retail sale is the sale of tangible personal property. It is also the sale of retail services such as installation, repair, cleaning, altering, improving, construction, and decorating. Other retail services include improving real or personal property, amusement and recreational activities, lawn maintenance, and physical fitness activities.

Sales tax amounts collected by the seller must be remitted to the Department of Revenue (DOR). The seller is liable to DOR for sales tax, whether or not it is collected.

Sales of food and food ingredients are exempt from retail sales tax. However, prepared foods, dietary supplements, soft drinks and bottled water are taxable. For more information on which food products are subject to sales tax, search for "When to Charge Sales Tax on a Food Item" on dor.wa.gov.

Retail sales tax includes both the state and local components of the tax. Sales tax rates are determined by the location where the buyer receives the goods. For example, a sale at a farm stand would use the tax rate where the farm stand is located. If a business ships or delivers merchandise within Washington, the location where the buyer receives the product determines the tax rate. It is the responsibility of the seller to charge the appropriate rate. There are some exceptions, such as sales of flowers through a Teleflora-type service. In these cases, the tax is based on where the item is sent from, and is called a "sourcing sales tax."

Looking Up Sales Tax Rates DOR has several tools to help businesses find the correct tax rates by location, including a "Tax Rate Look Up" mobile app and online search tool, dor.wa.gov/taxratelookup. Each time you look up a rate, record and track the confirmation code provided. You will need this confirmation number in the event of an audit. You will also use the location code and percentage when reporting the tax on the excise tax return.

3. Use Tax

Goods used in Washington are subject to either sales or use tax, but not both. The use tax compensates for when sales tax is not paid.

Use tax is determined on the value of the goods when first used in Washington. Generally, this is the purchase price. However, a depreciated value may be determined if the goods are used outside the state for a lengthy time before use in Washington by the same person. For example, if a farmer buys a tractor in Oregon (where there is no sales tax), they must pay a use tax on the current value at the time it comes into Washington.

For information on tax rates and how to pay, search for "Use Tax" at dor.wa.gov, or call 800-647-7706.

Sales Tax Exemptions for Farmers

Below is a listing of the most common sales tax exemptions available to farmers with a brief description. For more information, please search DOR website, dor.wa.gov, for the "Agriculture Tax guide"

- **Agricultural Employee Housing:** Sales tax does not apply to the material or labor used in the construction, repair, or improvement of agricultural employee housing.
- **Anaerobic Digesters:** Sales tax does not apply to the installing, constructing, repairing, cleaning and improving of an anaerobic digester.
- **Animal Pharmaceuticals:** Sales tax does not apply to animal pharmaceuticals sold to farmers when administered to farm animals.
- **Auction Sales of Farm Property:** Sales tax does not apply to tangible personal property bought or sold at a farm auction.
- **Chicken Bedding Materials:** Sales tax does not apply to materials used for chicken bedding.
- **Farm Fuel:** Fuel used strictly for farming purposes is exempt from sales tax.
- **Food and Food Ingredients Used for Human Consumption:** Exempt from sales tax, however this exemption does not apply to prepared food.
- **Replacement Parts:** Sales tax does not apply to the purchases of qualified replacement parts for farm machinery or equipment. This does not extend to the purchases of farm machinery or equipment.

Find a full list of exemptions on the DOR website, by searching for "sales tax exemptions," or contact DOR directly with questions about what goods and services are taxable.

Sales Tax Exempt Wholesale Purchases

To purchase goods at wholesale without paying sales taxes, farmers need one of the following, issued by DOR:

- Reseller permit for businesses that make a purchase for resale.
- Farmers' Certificate for Wholesale Purchases and Sales Tax Exemptions.

Farmers who have registered with DOR for the Farmers' Certificate for Wholesale Purchase can purchase certain goods without paying tax. Qualifying purchases specifically exempted by law include:

- Feed, seed, seedlings, fertilizer, pesticides, and spray materials.
- Items for resale.
- Agents for enhanced pollination including insects such as bees.

To use these certificates, you must be a farmer who produces an agricultural product for sale on land you own or have a present right of possession. You must provide a copy of the certificate to the vendor in order to purchase the eligible items without paying sales tax.

If you use either permit or certificate for sales tax exemptions, you must keep records of your purchases so DOR can verify that the purchases were qualified. For audit purposes, keep these records five years from date last used.



Litter Tax

Litter tax is a tax on manufacturers, wholesalers, and retailers of certain products which contribute to the litter problem in this state. Thirteen categories of products are subject to the litter tax, including food for human or pet consumption, packaged groceries, and the sale of glass, metal, or plastic containers and paper products.

Litter tax is reported on the excise tax return as a separate line item. The rate is 0.00015 of the taxable amount. The funds are used by Department of Ecology for a litter control program employing youth to clean up public places, and for public education and awareness programs relating to litter control and recycling.

For complete information, search for "Litter Tax" at dor.wa.gov, or call 800-647-7706.

Property Tax and Open Space Designations

Farmers may be liable for two types of property taxes: 1) real property tax, and 2) personal property tax. The tax rate for real and personal property is the same. If you own your land and buildings, you will be assessed for real property tax. Most farm equipment, machinery and supplies are subject to personal property tax. An exemption or partial exemption may apply to some farm machinery and equipment.

Property tax is administered by county governments. Contact the assessor's office in the county where the property is located for questions on property valuation, taxes, and tax exemptions. Search dor.wa.gov for "county assessor websites."

The Open Space Taxation Act, enacted in 1970, allows property owners to have their open space, farm, agricultural, and timber lands valued at their current use rather than at their highest and best use. The act states "it is in the best interest of the state to maintain, preserve, conserve, and otherwise continue in existence adequate open space lands for the production of food, fiber, and forest crops and to assure the use and enjoyment of natural resources and scenic beauty for the economic and social well-being of the state and its citizens."

Applications for open space classification can be submitted to county assessor's office where the property is located at any time during the calendar year. Current use valuation assessment begins on January 1 in the year following the application submission. Some jurisdictions may charge an application processing fee.

Find an information sheet with the details of the Open Space Taxation Act on the DOR website or call the Department of Revenue Taxpayer Assistance, Property Tax Division at 360-570-5900.

Washington State Labor-Related Taxes

State Payroll Taxes

If your farm has employees, you are responsible for state payroll taxes in addition to the federal payroll taxes. When you hire an individual as an employee (not an independent contractor) to work or perform a job for you, no matter how small the job is, you need to report that individual to the Washington Employment Security Department (ESD). There is no minimum dollar or hour threshold; all employees must be reported.

For complete information, contact the Washington Employment Securities Department at esd.wa.gov, or call 888-836-1900 for general employer tax information and forms. Please see the Labor Fact Sheet for more information on employer responsibilities.

Workers' Compensation Insurance

Employers are required to pay workers' compensation premiums for employees. This includes agricultural operations paying wages to family members over the age of 18. Payments go into the Worker's Compensation Fund managed by Washington State Department of Labor & Industries (L&I).

Workers' compensation is an insurance system to cover people hurt on the job. Benefits include medical care, time-loss compensation, permanent partial disability, vocational rehabilitation, pensions, and other payments. This tax assessment is based on the number of hours worked per particular work classification. The assessment is determined when a tax number called a Unified Business Identifier (UBI) is issued with a Washington State Business License. Individual employers can control costs by maintaining a safe work environment to minimize accident claims which can result in reduced premiums.

Labor & Industries has an "Employer's Introduction to Workers Compensation" webinar and other helpful information available by searching their website, lni.wa.gov.

State Unemployment Insurance Tax

Every business with employees in Washington State must register with the Employment Security Department (ESD) and file unemployment insurance tax, wage reports, and taxes every quarter.

Your account with ESD is established when you submit the Business License Application with the Department of Revenue (DOR) and indicate you have employees. Existing licensed businesses that are hiring employees for the first time need to establish an account with ESD by submitting a new State Business Application indicating you have employees. Be sure to include the Unified Business Identifier (UBI) number originally assigned from your first Business License Application. Contact ESD's Registration Unit, status@esd.wa.gov or 360-902-9360, to activate or inactivate your account as needed with changes in your status as having employees or not. Once your

business account is established, ESD will send you an account number and a tax rate notice. Use the online Employer Account Management Services (EAMS) for filing wage reports and paying unemployment taxes.

See the ESD website, esd.wa.gov, and search for "About EAMS" for information and guidance on how to plan, report wages, and pay for unemployment taxes, including how to use the all-in-one online filing tool.

When a former employee files for unemployment benefits, you will receive a "Benefit Charging Notice." It is essential that you respond to these notices when you can document a voluntary quit or discharge for misconduct. By responding to these notices with a "request for relief of benefits charges" your experience rating will not be charged if approved, and you may qualify for a lower tax rate the following year. Find more details in the "Benefit Charging Notice FAQ's" on the ESD website.



5. Licensing

9. Insurance

10. Labor on the Farm