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FEDERAL FARM INCOME TAXES
Is Treasury The Loser?

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Income tax

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U.S. farmers have been favored by the Federal Government through a variety of agricultural policies and programs that have attempted to raise product prices and incomes. These activities are well-documented throughout the literature of agricultural economics. Preferential treatment has also been associated with taxes levied on farm producers. The effects of tax policies on agriculture have already been analyzed to a considerable extent. For example, Davenport and others reviewed and summarized earlier work and discussed how tax policies have contributed to changes in the agricultural sector (2).

Several studies of probable effects of income tax law changes have relied on knowledge of the tax code and an understanding of the farm economy in modeling the impact of taxes. For example, Nixon detailed differences between Federal law and Treasury proposals and simulated tax and farm program provisions for representative farms.

This paper attempts to quantify the net effect on the U.S. Treasury of Federal income tax provisions by estimating taxes paid by those with farm net income or loss. The approach is to present summary data from a sample of about 15,000 Federal farm income tax returns of individuals for 1982. Information is provided on the significance of reported losses and on the widespread nature of loss reporting. The data provide evidence of a negative net flow of revenue from the U.S. Treasury to individuals with farming interests.[1] Although the frequent reporting of losses has been recognized, the impact on Treasury tax receipts has not been as evident.

All citizens and residents of the U.S. meeting certain minimum income levels must file a Federal income tax return.[2] However, several provisions of the tax law tend to lessen the Federal income tax burden on farmers.[3]

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Reporting Trends

As tax laws changed, nominal incomes increased, and off-farm income became relatively more important, the number of individuals and businesses reporting farm income or loss for U.S. Federal income tax purposes increased--from fewer than 2.8 million in 1945 to about 3.5 million by 1955 (table 1). Numbers reporting have been around three million in recent years, at least through 1980. Meanwhile, farm numbers declined from 6.0 million in 1945 to about 2.4 million during 1980 to 1982 (table 2).

Table 1—Farm Income Tax Returns, by Type of Business Organization, Selected Years, 1945-82[1]

Year	Individuals	Partnerships	Corporations	Total
	Thousands			
1982	[2]2,692	112	66	[2]2,870
1980	2,972	108	56	3,136
1975	3,122	110	40	3,272
1970	2,906	111	24	3,041
1965	3,064	116	19	3,199
1955	3,417	[3]	[3]	---
1945	2,659	97	[3]	---

[1]Based on U.S. Business Tax Returns and related data, Internal Revenue Service, U.S. Department of the Treasury.

[2]Not fully comparable with estimates for earlier years because certain crop share landlords who did not participate directly in the management were excluded from the sample in 1982. In 1980, there were an estimated 422,000 such landlords.

[3]Not available.

Table 2—USDA Estimates of Farms, Gross Cash Receipts and Net Cash Income from Farming, Selected Years, 1945-82

Year	Number of Farms[1]	Gross Cash Receipts[2]	Net Cash Income from Farming Less Depreciation[2]
	Mil.	Bil. Dol.	Bil. Dol.
1982	2.4	149	19
1980	2.4	143	20
1975	2.5	91	18
1970	2.9	55	12
1965	3.4	42	10
1955	4.7	30	9
1945	6.0	22	10

[1]National Agricultural Statistics Service, U.S. Department of Agriculture.

[2]Economic Research Service, U.S. Department of Agriculture, Economic Indicators of the Farm Sector, National Financial Summary, 1984, tables 3, 6, and 9.

Because the number of farm tax returns has exceeded the estimated number of farms in recent years, it is apparent that farm operators are not the only ones who file farm returns. For some farming operations, there are two or more returns because informal partners, family members, and owners of farmland or providers of labor and capital share in the income.[4] Differences may also occur because some of those with small amounts of farm income are not required to report for tax purposes when their total income is too low.

Business receipts reported on farm tax returns have increased from $16 billion in 1945 to about $152 billion in 1980 and perhaps near $160 billion in 1982 (table 3). During 1945 to 1980, gross cash receipts estimates of the U.S. Department of Agriculture (USDA)

Table 3—Farm Business Receipts Reported on Tax Returns by Type of Business Organization, Selected Years, 1945-82[1]

Year	Individuals	Partnerships	Corporations	Total
	Million Dollars			
1982[2]	99,300	3/	41,993	---
1980	94,679	19,173	38,242	152,094
1975	65,267	11,531	21,223	98,021
1970	39,144	6,158	8,995	54,297
1965	29,908	4,097	4,877	38,882
1955	20,779	3/	3/	---
1945	14,227	1,713	3/	---

[1]Based on U.S. Business Tax Returns and related data, Internal Revenue Service, U.S. Department of the Treasury.

[2]Not comparable with estimates for earlier years because certain crop share landlords, who did not participate directly in the management, were excluded from the sample in 1982. In 1980, such landlords reported receipts of $5.1 billion.

[3]Not available.

increased from about $22 billion to about $143 billion. Gross cash receipts were then estimated at $149 billion for 1982 (table 2).

Despite major differences in underlying concepts and in the way the data are produced, gross farm receipts reported to the Internal Revenue Service (IRS) and gross cash receipts from farming estimated by the USDA are sufficiently close to allay fears of massive underreporting. However, there are significant differences between net cash income estimated by USDA and net income shown in the tax data.[5] Those with farm income appear to minimize taxes mainly by using the relatively liberal provisions of the tax code.

Losses Reported in 1982

For tax year 1982, a sample of Federal income tax returns of individuals reporting net farm incomes or losses was prepared under an agreement with Internal Revenue Service (IRS). The data were supplied in summary form for analysis of farm tax policies and as supplemental information on the farm sector.[6]

Given the relatively favorable rules for reporting, it is not surprising that some U.S. farm proprietors list losses. As early as 1962, more than 30 percent of those with farm receipts reporting as individuals reported negative incomes from farming. Since then the percentage reporting losses has increased further so that by 1982 some 65 percent of such tax filers showed farm losses. Part of the increased incidence of losses may have been due to the difficult financial situation of the agricultural sector in recent years.

Reported farm losses far exceeded net farm income reported to IRS in 1982. Those reporting net farm income listed a total of about $8 billion; reported losses amounted to $18 billion. Therefore, the "net" farm sector "losses" for individuals were about $10 billion. By 1984, IRS estimated "net farm sector losses of about $12.7 billion (8, p. 85).

Net income of farm corporations reporting profits in 1982 was about $2.1 billion, but this was slightly more than offset by corporations reporting losses. Thus, in aggregate, net income of farm corporations was negative (6). Similar data are not available for partnerships. However, 1981 estimates by IRS show net losses for all farm partnerships of more than $600 million (7, p. 35).

It is not possible to sort out how much of the total reported loss on farm tax returns is attributable to peculiarities of the tax law and that which might be termed economic loss. A rough measure is the difference between the net cash income estimates of the USDA, less depreciation, and net amounts reported for tax purposes. For 1982, net cash income from farming, less depreciation, was estimated by USDA at about $19 billion (table 2). This contrasts with the $10 billion net sector losses reported for that year on farm tax returns of individuals. And, the $10 billion neglects losses of farm corporations and partnerships.

Not only are farm losses large, but regardless of how the numbers are summarized those reporting losses dominate the data. For example, when individuals with farm income are classified by amount of farm receipts, each of eleven classes reported a net loss (table 4). In many but not all of the classes, more taxpayers reported losses than positive net income from farming. The percentage reporting losses was largest for those with the smallest farm business receipts, but as would be expected average losses were greater for each successively higher receipts level.

From the perspective of type of farm as coded by IRS using Standard Industrial Classification Codes, results were consistent with those by receipts classes (table 5). Only two farm business types reported greater farm profits than farm losses. Some two-thirds of individuals classified in horticultural specialties, which include primarily ornamental floriculture, nursery products, and food crops grown under cover, reported losses. However, their reported losses were relatively small and net income less losses for such farms was only slightly positive.

About sixty percent of those classified in dairying reported positive incomes. This may be partly explained by the more limited opportunity to shift dairy receipts and expenses between tax years because of their regularity. Also, because dairy farms are labor intensive, individuals involved have been found to have less off-farm income. They would thus have less incentive for seeking tax shelters. Finally, the relatively favorable Government programs for dairy enterprises in 1982 could have played a role.

Earlier studies have shown that many of those with substantial off-farm incomes report farm losses for tax purposes (Carlin). Also, those with the greatest off-farm incomes generally have been shown to report larger losses. The 1982 data show 85 percent of individuals with the highest level of off-farm income--$50,000 or more--reporting losses, averaging nearly $25,000 (table 6). As expected, lower percentages reported farm losses among individuals with off-farm incomes of less than $25,000. About four-fifths of the $65 billion total off-farm income and capital gains reported on the Federal tax returns of individuals reporting farm profits or losses went to those with losses.

Table 4--Individuals Reporting Farm Income or Loss by Amount of Farm Business Receipts, 1982[1]

Amount of Receipts	Number Reporting 2/	Net Income Less Loss	Percent Reporting Net Farm Income	Average Net Farm Income	Percent Reporting Net Farm Loss	Average Net Farm Loss
	Thou.	Mil.Dol.	Pct.	Dol.	Pct.	Dol.
No reported farm receipts	227	-1,286	---	---	100	5,674
Less than $2,500	678	-2,183	19	646	81	4,107
$2,500 to $4,999	306	-1,192	27	1,381	73	5,829
$5,000 to $9,999	318	-1,259	37	2,779	63	7,895
$10,000 to $24,999	370	-1,628	42	4,378	58	10,664
$25,000 to $49,999	276	-925	52	7,776	48	15,541
$50,000 to $99,999	268	-140	61	12,731	39	21,201
$100,000 to $249,999	190	-287	41	20,718	59	34,123
$250,000 to $499,999	40	-290	61	30,406	39	65,129
$500,000 to $999,999	11	-166	52	50,977	48	87,218
$1,000,000 or more	5	-478	44	97,686	56	235,019
Total	2,689	-9,834	35	8,568	65	10,151

1/Based on special tabulations prepared by Internal Revenue Service, U.S. Department of the Treasury.

2/Excludes returns with net equal to zero.

Table 5--Individuals Reporting Farm Income or Loss by Type of Farm, 1982[1]

Type of farm	Number Reporting 2/	Net Income Less Loss	Percent Reporting Net Farm Income	Average Net Farm Income	Percent Reporting Net Farm Loss	Average Net Farm Loss
	Thou.	Mil. Dol.	Pct.	Dol.	Pct.	Dol.
Field Crop	1,233	-3,262	37	9,283	63	9,784
Vegetable and Melon	54	-107	42	10,295	58	10,793
Fruit and Tree Nuts	79	-380	32	13,046	68	13,202
Horticultural Specialities	10	4	33	8,734	67	3,609
Beef Cattle Feedlots	4	-35	14	14,097	86	12,353
Beef Cattle Except Feedlots	720	-4,823	26	5,585	74	10,968
Hog, Sheep, and Goats	204	-193	41	8,649	59	7,708
Dairy	179	112	60	9,890	40	13,376
Poultry and Eggs	46	-104	37	6,535	63	7,354
General Livestock, Except Animal Specialities	21	-68	28	8,829	72	7,784
Animal Specialities	64	-596	15	4,990	85	11,925
Farms not allocated	75	-382	13	7,124	87	6,842
Total	2,689	-9,834	35	8,568	65	10,151

1/ Based on special tabulations prepared by Internal Revenue Service, U.S. Department of the Treasury.
2/ Excludes returns with net equal to zero.

Table 6--Individuals Reporting Farm Income or Loss by Amount of Off-Farm Income, 1982[1]

Amount of Off-Farm Income	Number Reporting	Net Farm Income Less Loss	Percent Reporting Net Farm Income	Average Net Farm Income	Percent Reporting Net Farm Loss	Average Net Farm Loss
	Thou.	Mil. Dol	Pct.	Dol.	Pct.	
Less than $25,000	1,756	-1,685	44	8,632	56	8,516
$25,000-$49,999	676	-3,248	18	6,408	82	7,210
$50,000 or more	260	-4,900	15	13,790	85	24,782
Total	2,692	-9,834	35	8,568	65	10,137

1/ Based on special tabulations prepared by Internal Revenue Service, U.S. Department of the Treasury.

While not from a precisely matching sample, a summary of individual returns data for 1981 showed more than 2.6 million individual returns with farm profit or loss. Net losses exceeded positive net by $7.8 billion. Losses were greater than net incomes in all but nine of the fifty states--again confirming the prevalence of loss reporting. Because overall farm losses were greater in 1982, it would not be surprising if losses exceeded net income in even more states during that year (5).

Individuals with farm net incomes or losses in 1982 were classified by amount of taxable income from all sources. The classes which were used match increments in the tax rate schedule for married taxpayers filing joint returns (table 7). Tax liability was computed for each taxable income class for proprietors with farm net incomes (column 1), farm net losses (column 3), and for all individuals with farm income or loss (column 5).

Next, for each individual tax return, farm net income or farm loss was excluded from income and the individuals were reclassified by amount of taxable income from other sources. Then the amount of tax liability was recomputed (columns 2, 4, and 6). Thus, the total line on table 7 shows that tax liability on farm proprietor returns with reported net income would fall from about $3.6 billion to about $2.1 billion if no taxes were due on the net income from farming. The difference of $1.5 billion represents an estimate of tax liability on positive net farm income of individuals in 1982.[8] Likewise taxes were recomputed for each taxpayer reporting farm losses. The estimated tax liability increased from about $7.6 billion to nearly $12.9 billion or by about $5.3 billion when farm losses were excluded from the calculation.

Combining returns with net farm income and losses (columns 5 and 6, table 7), it is evident that the U.S. Treasury lost revenue to individuals involved in farming. In other words, if farm income had not been taxed and farm losses had not been used to reduce taxes on other income the total tax received by the Treasury would have been an estimated $3.8 billion greater ($15,004 million minus $11,211 million). Again, this estimate does not include farm partnerships and corporations.

Table 7—Tax Liability of Individual Farm Proprietors by Amount of Taxable Income, 1982 1/

Amount of Taxable Income 2/	Amount of Tax Liability: Proprietors with Farm Net Income		Proprietors with Farm Net Loss		All Farm Proprietors 3/	
	Tax Including Farm Net	Tax Excluding Farm Net	Tax Including Farm Loss	Tax Excluding Farm Loss	Tax Including Farm Net and Farm Loss	Tax Excluding Farm Net and Farm Loss
	Million dollars					
Less than $3,400	1	2	6	1	7	3
$3,400-5,499	13	9	15	15	28	23
$5,500-7,599	30	22	40	40	70	62
$7,600-11,899	122	88	187	204	309	292
$11,900-15,999	152	97	261	318	412	415
$16,000-20,199	218	122	416	488	635	610
$20,200-24,599	245	135	529	693	774	828
$24,600-29,899	286	147	568	844	854	991
$29,900-35,199	223	135	543	856	765	992
$35,200-45,799	420	215	759	1,382	1,179	1,597
$45,800-59,999	359	158	534	1,072	893	1,230
$60,000-85,599	465	237	527	1,213	993	1,450
$85,600 or more	1,116	775	3,176	5,736	4,292	6,511
Total	3,650	2,142	7,561	12,862	11,211	15,004

1/Based on special tabulations prepared by Internal Revenue Service, U.S. Department of the Treasury.
2/These taxable income classes are based on the schedule of tax rates for married taxpayers filing joint returns (schedule Y).
3/Individual values may not sum to totals because of rounding.

Summary and Conclusions

This paper has presented statistics derived from samples of U.S. Federal income tax returns of those filed for 1982 by individuals participating in farm production. For that year, the Treasury in its effort to tax farm income is shown to have lost about $3.8 billion to those involved in farming. While those involved in farming are not the only beneficiaries of special tax provisions, questions can be raised about the tax code as applied to the farm sector. It is by no means clear that those mainly dependent on farming for their livelihood gain the most. Regardless of how the data are summarized, reporting of farm losses was found to be commonplace. Each farm receipts class from less than $2,500 through $1 million or more showed losses on net from farming. Only two of the identified farm types listed greater net income than losses. Farm losses also seem to be related to the importance of off-farm income. Finally, similar data for 1981 show reporting of losses to be geographically widespread.

Footnotes

[1]IRS uses the term sole proprietor rather than individual.

[2]Minimum income requirements have increased over time.

[3]These provisions are discussed elsewhere and will not be repeated here (2). Special provisions also are available to other segments of the population.

[4]Farm returns discussed here exclude farm wage workers.

[5]Studies by Treasury indicate that proprietorship income is often underreported (4). Comparison of receipts estimated by USDA and IRS suggests otherwise.

[6]No individual records were provided. While farm partnership and corporation data would also be of interest such detailed information is not available for those business organization forms.

[7]Treatment of capital gains and losses separately from farm receipts probably increased reported losses.

[8]There is an inherent assumption that farm income is taxed at the individual's highest marginal tax rate.

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