ALTB 04-05 AGRICULTURAL LABOR TAXATION

Abstract
Some laws regarding payroll taxes for agricultural labor are different than those for other types of businesses. The following will explain these differences so a farmer can report his farm labor correctly. This article covers major differences but is not intended to be complete or to cover state law.

Reporting Requirements

Overview
Hiring of employees subjects the employer to many state and federal regulations and reporting requirements. In agriculture, many smaller operations are exempted. However, as farms increase in size and additional employees are hired, more requirements will apply.

Reporting Requirements
Determining Who is an “Employee”
For reporting requirements to apply, the person rendering the services for a farmer must be an employee as defined either under state common or statutory law. In general, to be classified as an employee, the employer must exercise control over the method and manner in which the assigned task is to be carried out. If the person rendering the services controls how the services are to be performed, the person is likely classified as an independent contractor. The line between independent contractor and employee is ultimately a factual determination. For tax purposes, if an individual is determined to be an employee, the employer is responsible for withholding and paying employment taxes for the employee. That is not the case for independent contractors.

Many agricultural operations have employees that serve as farmworkers. That is the case particularly for operations that employ laborers to raise or harvest agricultural or horticultural products, or work in connection with the operation, management, conservation, improvement, or maintenance of the farm and its tools and equipment. Likewise, agricultural operations that process or package commodities on site typically hire laborers to perform the processing or packaging tasks. However, more than 50% of the commodities must be produced on site. Also, houseold labor that is hired to do housework in the employer’s private home located on a farm operated for profit is handled under the same rules.

Note. For the purpose of determining whether a person is a farmworker, labor services must be rendered on a farm, including stock, dairy, poultry, fruit, fur-bearing animal, and truck farms. A “farm” also includes plantations, ranches, nurseries, ranges, greenhouses, or other similar structures used primarily for the raising of agricultural or horticultural commodities and orchards. However, “farmwork” does not include reselling activities that do not involve any substantial activity of raising agricultural or horticultural commodities, such as a retail store or a greenhouse used primarily for display or storage.
Employment Taxes

Cash wages paid to agricultural employees are subject to social security, Medicare, and income tax withholding. Commodity wages are not cash wages and are not subject to social security, Medicare, or income tax withholding. The employer must report the FMV of the in-kind payment as income and may deduct an equal amount of wage expense. The FMV of the in-kind payment is included in the employee’s income as W-2 income, and the employee has a basis in the commodity equal to that value. When the employee later sells the commodity, gain or loss will be triggered depending on whether the sale price exceeds, equals, or is less than the basis of the commodity. The resulting gain or loss is reported on Schedule D if the employee is not a dealer in the commodity and does not sell the commodity in the course of a farm business. If the employee is a dealer or a farmer, the sale should be reported on Schedule C or Schedule F, respectively. If the employee uses the commodity in the employee’s farming operation, the employee is entitled to a Schedule F deduction for the basis.


Social security and Medicare taxes also do not apply to wages paid to share farmers or to alien workers admitted under section 101(a)(15)(H)(ii) (a) of the Immigration and Nationality Act on a temporary basis to perform agricultural labor.

Note. Meals and lodging furnished for the employer’s convenience under IRC §119 are not wages for FICA or FUTA purposes. However, they are wages for FICA and FUTA purposes if they are not provided for the convenience of the employer.

In general, wages paid to family members as employees are subject to social security, Medicare, and income tax withholding, as well as FUTA tax. But certain exceptions may apply for a child, spouse, or parent of the taxpayer.

- Children as employees: Wages paid to children under age 18 who work for a parent in a trade or business are not subject to social security and Medicare taxes. If the child performs domestic work in the parent’s home, the child’s wages are not subject to social security and Medicare taxes until the child reaches age 21. In any event, the child’s wages are not subject to FUTA tax until the child reaches age 21. Wages for nonfarm work, however, may still be subject to income tax withholding.

- Spouse employed by other spouse: Wages paid to a spouse who works for the other spouse in a trade or business are subject to social security and Medicare taxes, but not FUTA tax. If the wages are for domestic services in a private home, they are not subject to social security, Medicare, or FUTA tax.

- Special rules apply to wages for the services of a child or spouse if they are employed by a corporation controlled by the parent or spouse, a partnership if the child’s parent is a partner (unless the only partners are the parents of the child), a partnership if the individual’s spouse is a partner, or an estate if it is the estate of a
deceased parent. In these situations, wages are subject to income tax withholding, social security, Medicare, and FUTA tax.

**Note.** Wages paid to a child of a sole proprietor or to a person who is a child of all partners in a partnership or all members of an LLC are not subject to social security and Medicare taxes. The wages should be reported on Form W-2 with no wages or tax showing in the social security and Medicare boxes. They should not be reported on Form 1099.

**Social Security and Medicare Taxes**

All cash wages paid to agricultural labor paid during the tax year are subject to social security, Medicare, and income tax withholding if either:

1. Cash wages are paid to an employee of $150 or more in a year for farmwork (including all cash wages paid on a time, piecework or other basis), or
2. The total the employer pays for farmwork to all employees (cash and noncash) is $2,500 or more during the year.

However, the above tests do not apply if the farmworker:

- is employed in agriculture as a hand-harvest laborer,
- is paid piece rates in an operation that is usually paid on a piece-rate basis in the region of employment,
- commutes daily from home to the farm,
- and had been employed less than 13 weeks in the preceding calendar year.

Amounts paid to these workers do count toward the $2,500-or-more test to determine whether wages paid to other farmworkers are subject to social security and Medicare taxes. Also, cash wages paid to a household employee are counted in the $2,500 test, but are not subject to social security and Medicare taxes unless the employer has paid the worker $1,400 or more in cash wages.

**Withholding Rules**

In general, farmers and crew leaders must withhold Federal income tax from wages paid to farm workers if the wages are subject to social security and Medicare taxes. The amount to withhold is computed on gross wages paid without withholding social security and Medicare taxes, union dues, insurance, or other deductions. Form W-4 is used to compute withholding allowances and to report other vital employee information to the employer.

A farm employer may decide to pay the employee’s share of social security and Medicare rather than to withhold it from the employee. There is a special rule for farmers requiring them to report the amount that should have been withheld as additional wages for income tax. However, they do not have to report this amount as additional wages for social security and Medicare.
Deposit Requirements

Employers must deposit both the employer and employee social security and Medicare taxes and income tax withheld (minus any advance earned income credit payments) during the year by mailing or delivering a check, money order, or cash to an authorized financial institution or Federal Reserve Bank. Some employers must deposit by electronic funds transfer. An exception from the deposit requirement exists if the employer’s net tax liability for the year is less than $2,500, or the employer is making a payment in accordance with the Accuracy of Deposit rules.

Federal Unemployment Tax Act (FUTA) Tax

In certain situations, agricultural employers are liable for FUTA tax. Employers who employ agricultural labor are subject to FUTA if they:

1. Paid cash wages of $20,000 or more in any calendar quarter during the current or preceding calendar year to persons employed in agricultural labor, or
2. Employed ten or more persons in agricultural labor for some portion of the day on each of 20 weeks during the current or preceding calendar year with each day being in a different calendar week.

**Note.** The spouse and children under age 21 of a farmer are not taken into account in determining whether the $20,000 of wages were paid or whether ten persons were employed in 20 different calendar weeks.

**Observation.** The FUTA tax rate is 8.0% on a wage base of $7,000. A credit is given for timely paid state employment taxes. Normally the net tax equals .8% or $56 per employee. The tax is reported on Form 940 or Form 940-EZ.

FUTA tax must be deposited with an authorized financial institution or the nearest Federal Reserve bank branch. Form 8109 must be submitted with each deposit.

FUTA tax liability must be computed on a quarterly basis to determine if a deposit must be made. Deposits must be made at the end of each calendar quarter only if the employer’s aggregate undeposited FUTA tax liability for the calendar year exceeds $100.

**Note.** Employers of aliens admitted to the U.S. on a temporary basis to perform agricultural labor must pay FUTA tax with respect to income earned by the alien workers if the other conditions for FUTA tax liability are satisfied. But non-resident aliens lawfully admitted to the U.S. on a temporary basis are exempt from FUTA, federal income tax withholding, social security, and Medicare tax when performing agricultural labor. These wages are included in the $20,000 and 20-week test.

Filing Requirement

Agricultural employers must file Form 943 on an annual calendar year basis. Form 943 is to be filed for all taxable wages paid to agricultural labor or to domestic employees. Employers employing nonagricultural labor must file Form 941 on a quarterly basis.
**Note.** Because the rules differ for agricultural and nonagricultural labor, it is important to use the correct form. The IRS attempts to send a Form 943 to each employer annually. The form is relatively simple to complete.

**Example 1.** Elmer Smith owns and operates his farm as a sole proprietorship. He employs Jeff on a full-time basis for $35,000 per year. Jeff works about 2,500 hours per year. Elmer also hires part-time help on a seasonal basis. In 2003, Elmer hired five other persons who worked a total of 400 hours spread out over 30 days during a 10-week period. These additional workers were paid an hourly wage of $5.00 per hour and earned a total of $2,000 in 2003. Elmer expects to hire about the same number of additional workers (besides Jeff) for approximately the same amount of hours in 2004.

**Question.** Are the additional workers independent contractors or employees?

**Answer.** Without more facts, it is difficult to tell. The answer will depend on the type of work being done and whether Elmer controls the method and manner in which the tasks are to be completed. However, Jeff is likely Elmer’s employee.

**Question.** Must Elmer pay FICA tax on the wages?

**Answer.** Because Elmer satisfies the $2,500 total payroll threshold, all of the wages he pays to all of his workers are subject to FICA taxes. While an exception for hand harvesters could possibly apply, it does not apply in this instance because Elmer does not pay his workers on a piece-rate basis. Therefore, Elmer will need to withhold 6.2% of the wages for the employee’s share of social security and pay his 6.2% share of social security on the wages. Elmer must also withhold 1.45% of the wages for the employee’s share of Medicare plus pay his 1.45% share.

**Note.** Elmer will also need to withhold federal income tax because the wages are not exempt from FICA tax. Thus, Elmer should have each employee sign a Form W-4 at the time employment begins. Elmer will also need to deposit federal employment taxes monthly and file an annual Form 943. However, Elmer will not be required to pay FUTA tax on the wages he pays to his workers.