

Pages 1 and 3 are to be filled in by farmers who either keep no records or only records of cash receipts and disbursements. Pages 2 and 3 are to be filled in by farmers who keep complete accounts on an accrual basis with inventories to determine net profits. Returns on an inventory basis are not acceptable unless the inventories were actually taken and so recorded at the beginning and end of the taxable period.

If you do not, as a matter of settled practice, keep books of account upon an accrual basis, no attempt should be made to fill out the items in the form relating to inventories, and the omission of those items in that case will not result in an incorrect computation of your farm net profit. If, however, you regularly keep books of account upon an accrual basis, which clearly reflect your net income, you should report the value of your crops and stock on hand at the end of the year in gross profits, as provided on the form.

This schedule may be used by farmers who work their own farms or rent them out on shares, and if two or more farms are owned it may be desirable to fill out a separate schedule for each farm.

Attach this schedule to your income tax return (Form 1040A or Form 1040). You should keep a copy for future reference.

When you have determined the net farm profit, transfer the amount to Item 5 of the income tax return Form 1040A, or Form 1040.

CASH RECEIPTS AND DISBURSEMENTS BASIS.

A farmer reporting on the basis of cash receipts and disbursements shall include in his gross income for the taxable year the amount of cash or the value of merchandise or other property received from the sale of live stock and produce which were raised during the taxable year or prior years, also the profits from the sale of any stock or other items which were purchased. The farm expenses will be the actual amounts paid out during the taxable year.

ACCRUAL BASIS.

If your farm books of account are kept on an accrual basis, the filing of this form is optional.

For those reporting on the accrual basis, the gross profits are obtained by adding to the inventory value of live stock and products on hand at the end of the year the amount received from the sale of stock and products and other miscellaneous receipts, for hire of teams, machinery, etc., during the year, and deducting from this sum the inventory value of stock and products on hand at the beginning of the year plus the cost of stock and produce purchased during the year. The farm expenses will be of the actual expenses incurred during the year, whether paid or not.

Inventory.—If you render a return for the taxable period of 1921 upon an accrual basis, you may value the closing inventory for 1921 according to the farm price method, which contemplates valuation of inventories at market less cost of marketing. In the event the use of the farm price method of valuing your closing inventory for 1921 represents a change in method of taking inventories from that employed by you for 1920, the opening inventory for 1921 should be brought in at the same value as the closing inventory for 1920 (this being the same in effect as valuing the opening inventory on the new basis and crediting income with the excess valuation brought in). If such treatment of your opening inventory for 1921 results, however, in an abnormally large income for 1921, then adjustments in the form of an adjustment sheet attached to your 1921 return may be made of your taxes for 1917 and each succeeding year to 1921, based on the new method of taking inventories (using for each of such years prior to 1921 the same method employed for 1921).

Farmers may change the basis of their returns from that of receipts and disbursements to that of an inventory basis, which necessitates the use of opening and closing inventories for the year in which the change is made. There should be included in the opening inventory all farm products (including live stock) purchased or raised, which were on hand at the date of the inventory, and there must be submitted with the return for the current taxable year an adjustment sheet for 1917 and each year thereafter (prior to the year in which the change is made) based on the inventory method; upon the amount of which adjustments the tax shall be assessed and paid (if any be due) at the rate of tax in effect for each respective year. Where it is impossible to render complete inventories from the beginning of the taxable year 1917, the Department will accept estimates which, in its opinion, substantially reflect the income on the inventory basis, for the year 1917 and thereafter; but inventories must not include real estate, buildings, permanent improvements or any other assets subject to depreciation.

INCOME.

All the farm income from whatever source must be reported in this schedule. Anything of value received instead of cash must be treated as income to the extent of its cash value. Thus, the total value of groceries, merchandise, etc., received in exchange for eggs, butter, or other produce must be reported as income.

Hail and fire insurance on growing crops should be included in gross income to the amount received in cash or the equivalent for the crop destroyed.

If you sold your farm or any part of it, report the profit in Item 6 of Form 1040A or Form 1040.

The value of farm produce which is consumed by the farmer and his family need not be reported as income; but expenses incurred in raising produce thus consumed must not be claimed as deductions.

The term "farm" embraces the farm in the ordinarily accepted sense, and includes stock, dairy, poultry, fruit, and truck farms, also plantations, ranches, and all land used for farming operations. All individuals, partnerships, or corporations that cultivate, operate, or manage farms for gain or profit, either as owners or tenants, are designated farmers. A person cultivating or operating a farm for recreation or pleasure is not regarded as a farmer.

EXPENSES AND OTHER DEDUCTIONS.

Labor.—Only that part of the board of hired labor which is purchased should be included as a deduction. The value of products furnished by the farm and used in the board of hired labor is not a deductible expense. Rations purchased and furnished to laborers or share croppers are deductible as a part of the labor expense. Do not deduct the value of your own labor or that of your wife or dependent minor children, unless you report such value as income in Item 1, Form 1040A or Form 1040. Do not deduct amounts paid to persons engaged in household work, except to the extent that the services of such employees are used in boarding and otherwise caring for farm laborers. Services of such employees engaged in caring for the farmer's own household are not a deductible expense.

Fertilizers, manures, etc.—The cost of manures, commercial fertilizers, lime, raw rock phosphate, etc., that were bought during the year may be deducted as an expense.

Taxes.—Do not deduct Federal income taxes nor taxes for any improvement or betterment tending to increase the value of the property. (See Articles 131 to 135, Income Tax Regulations, 1922 edition.) Be ready to show tax receipts for taxes claimed as a deduction. Taxes on your dwelling or household property should be reported in Item 11, Form 1040A, or Item 13, Form 1040.

Interest on indebtedness.—All interest paid on farm mortgages, notes, and other obligations incurred to carry on the farm business should be deducted.

Bad debts.—Report only debts, or portions thereof, arising from sales that have been reported as income, which have been definitely proved within the year to be worthless, or such reasonable amount as has been added to a reserve for bad debts within the year. If you report your farm income on a cash basis, bad debts arising from sales are not an allowable deduction.

Repairs and depreciation.—Depreciation claims should not exceed the actual cost of buildings and equipment (or if acquired prior to March 1, 1913, the fair market value on that date) divided by its probable life in years since acquisition. In computing depreciation do not include the value of farm land nor the land on which farm buildings are located. Do not deduct repairs or depreciation on the dwelling you occupy or on your personal or household equipment. Do not claim as a separate item depreciation on live stock or any other property included in your inventory, as such depreciation is taken care of in the reduced amount of the inventory at the close of the year. Depreciation, however, may be claimed on draft or work animals and animals held for breeding purposes which were purchased and which are not included in your inventory of stock bought or raised for sale.

Losses.—You may deduct in Item 12, Form 1040A, or Item 14, Form 1040, losses of buildings, machinery, and other property not included in your inventory, resulting from fires or other casualties and not compensated for by insurance or otherwise. Losses of property included in your inventory are taken care of by the reduced amount of the inventory at the close of the year. The loss of growing crops by frost, storm, flood, or fire, or the loss of animals raised, is not deductible.

Tools, machinery, and equipment.—The cost of small tools of short life, such as shovels, rakes, etc., may be deducted as an expense. You may deduct expenses of operation, repairs, and depreciation on automobiles used exclusively in farm business. If an automobile is used in farm business for a part of the time only, a corresponding part of the expense may be deducted. Amounts expended for automobiles, farm machinery, farm buildings, or other farm equipment of a permanent nature are not deductible as expenses, as such expenditures are regarded as investment of capital which is returned to the owner through depreciation allowances prorated over the useful life of the property.

Rent paid in crops.—Where a tenant farmer pays his rent to the landlord in form of crops raised on the farm (the agreement being on a crop-share basis), the tenant may not deduct as rent the value of the crop given to the landlord, but he may deduct all amounts paid by him in raising the crop.