

CONTRYMAN  
Associates, P.C.

# The Contryman Farm Account

Spring  
2005

*The Family Farm*

## Planning Transfer of Ownership

*Editor's Note: In January Contryman Associates and several other businesses in Central Nebraska hosted a farmer appreciation event in Hastings. Speaker for the event was a CPA from Washington State, Chris Hesse. He made his presentation on transferring ownership of the family farm to more than 300 guests. The slides he used with his presentation are available on the Contryman web site, [www.capc.com](http://www.capc.com)*

*In this copy of The Contryman Farm Account we will summarize some of the points he made in his presentation. If you have questions or need help with your own succession or estate plan, contact a Contryman office.*

### Fair vs. Equal

A key issue when planning for succession of the family farm is the concept of "fair" vs. "equal." Families often consider which family members have contributed to the overall growth of the estate while making the distribution fair to other family members. Some family members may have extraordinary needs (medical, education, charitable) to consider. And, personal philosophies will always influence estate planning decisions.

Most farming operations include both operating assets and non-operating assets. One strategy is to transfer operating assets (crop land, equipment, livestock, etc.) to family members who are active in the operation. Transfer non-operating assets (house, non-work vehicles, etc.) to other family members.

If more than one family member is active in the farming operation, they may prefer that separate operating entities be established.

### Transfer Now or Later

Another consideration is whether to transfer ownership now or later. Earlier transfer allows parents the joy of watching their children become successful. However, younger children may make mistakes that could have been avoided if the transfer had been made later.

In his January presentation to farmer friends of Contryman Associates, speaker Chris Hesse, CPA, commented that one of his clients told him he didn't want to transfer ownership to his son yet because he wasn't sure he could be trusted to make decisions for the farming operation. "After all, he's only 60!" said the father.

If ownership is transferred earlier, parents are cautioned that real estate will provide a more stable retirement income than operating assets. Those providing the management and labor should be rewarded appropriately and should not be expected to cover extraordinary medical and living needs. It is important that sufficient coverage be in place for these unexpected expenses.

### Selling or Giving Assets

Depending on the situation, selling the farming assets to your successor may require that you pay either capital gains or ordinary income tax on the proceeds. Selling assets on installments provides cash flow for the parent and only the amount paid in each year is taxed. The buyer receives an increase in tax basis for

depreciation purposes, a benefit not enjoyed when assets are gifted to successors.

When assets are gifted, no income tax must be paid on the receipt. However, if certain gifts of property are received and then sold, there may be income tax due on the gain. No gift tax is paid if gifts are given within the annual gift tax exclusion.

Assets that are transferred through an estate get a stepped up basis that eliminates gain if property is sold immediately after death. This stepped up basis concept is the reason there is a natural reluctance to gift or sell property to the next generation.

Section 1031 exchanges of like-kind property are an option if diversification is desired. There is currently no income tax paid on these exchanges. While properties being exchanged need not be the same, there are qualifications that must be met.

### Transferring Future Growth to the Younger Generation

You can create opportunities for children to receive the increase in wealth through operating partnerships where children receive guaranteed payments for current earnings. Withdrawals by the older generation create effective redemption of partnership interest. This process allows gifts of partnership interests while the older generation maintains control. Upon death, discounts are available.

Real estate partnerships allow children to own the operating entity while keeping rents low. This may be a mechanism for giving of

Contributing information for articles in this issue are Contryman farm tax professionals and these shareholders:

**Joel Wiegand, CPA**

Grand Island Office Managing Shareholder

**Chris Oppliger, CPA**

Hastings Office Managing Shareholder

**Marlin Johnson, CPA**

Lexington Office Managing Shareholder

**Rachelle Bryant, CPA**

Kearney Office Managing Shareholder

**Dan Charron, CPA**

Scottsbluff Office Managing Shareholder

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Certified Public Accountants

# CONTRYMAN ASSOCIATES, P.C.

Grand Island	308-382-5720
Hastings	402-463-6711
Lexington	308-324-2368
Kearney	308-237-5930
Scottsbluff	308-635-7705
Central City	308-946-3870
Geneva	402-759-3002

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Thank you for referring us to your friends and family members.

## Planning for Transfer of Ownership of the Family Farm

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partnership interests to non-active family members when other non-farm assets are not available.

Another option would be for older generation family members to lend money to children so they can purchase the business.

### The Federal Estate Tax

Federal estate tax exemptions are rising at this time and the tax is slated to be repealed in 2010. However, in the year 2011, the estate tax is reinstated unless Congress acts to

change current law. Additionally, more states, including Nebraska, are "de-coupling" from the Federal estate tax, no longer basing their taxes and exemptions on federal estate laws. State inheritance taxes must be considered when planning for the estate. Remember that your estate includes not only land and other obvious assets of the farm but all of your assets including life insurance, retirement plan proceeds, and interests in corporations, partnerships, and trusts.

### Conclusion

While many suggestions for planning for the transfer of the family farm were offered by Mr. Hesse in his presentation and recounted in this article, you are advised to seek the help of an estate planning professional. The role that Contryman Associates CPAs play in developing an estate plan is to look at your family's unique situation and address all aspects of planning for the succession of your family farm with the goal of minimizing taxes and providing peace of mind for all family members.

The number of U.S. farms operated by full-time farmers has dropped more than 21% and the average age of farmers increased from 49.4 to 52.5 year of age from 1987 to 1997. Slightly more than 15% of Nebraska farms are owned by people age 70 or older.

## Beginning Farmer Tax Credit Program

- The Nebraska Beginning Farmer Tax Credit Act was established in 1999 to encourage present farmers and ranchers to offer beginning farmers and ranchers a needed start in their industry.
- The program works like this: The owner of an agricultural asset, such as land, livestock facilities, machinery, livestock, etc., may agree to rent or lease the asset for three years to a beginning farmer or livestock producer. The rent may be based on cash rent, share-crop, cow-calf shares, etc. The owner will receive a refundable tax credit equal to five percent of the amount of rent received each year for three years on each rented asset. There is an application and eligibility approval process. A summary of qualifications are listed below
- For more information, and a copy of the entire Beginning Farmer Tax Credit Act go to the Nebraska Department of Agriculture's web site or find a link on the Contryman Associates web site at [www.capc.com](http://www.capc.com).

### A Qualified Beginning Farmer/Livestock Producer Will:

- Be a resident of Nebraska with a net worth of not more than \$100,000.
- Be actively involved in livestock/farming and seeking to make a livelihood in the sector.
- Provide the majority of day-to-day physical labor and management on the farm.
- Have livestock/farming experience or education.
- Participate in a Board approved financial management educational program.
- Not be related to the owner of the rented assets
- Have farmed or raised livestock for less than ten of the past fifteen years.

### A Qualified Farm/Livestock Asset Owner Will:

- Be a resident of Nebraska and be eligible to receive a state income tax credit.
- Have derived at least 50% or more of his/her gross annual income for income tax purposes from farming or livestock production.
- Have provided the majority of the day-to-day physical labor and management of a farm or livestock production for five of the last fifteen years.
- Not be related to the beginning farmer or livestock producer.

The State of Nebraska is concerned about the retention of young farmers who are facing many financial problems today. Many farmers and ranchers have viable operations and do not have family members working with them or taking over for them. Also, there are many part-time farmers and ranchers who lack the opportunity to rent available land and livestock operations that will support a family.

The Beginning Farmer Program will help ensure success for both asset owners and young farmers.

### The Contryman Farm Account Newsletter

The **Contryman Farm Account** has been developed to address issues specific to the needs of our farmer friends and clients. It will be sent to you free of charge several times each year. Also, if you have farmer friends or relatives that you believe would benefit from the information in the **Farm Account**, please let us know and we will add them to our mailing list. If you would prefer not to receive this publication, we will be happy to remove your name.

*The technical information in this newsletter is necessarily brief. No final conclusion on these topics should be drawn without further review and consultation with a tax professional. For additional information, contact our firm.*