



Workbook

for

**Farm/Ranch Transition
When You Aren't
In Control**

<http://go.unl.edu/FarmRanchTransition>

Fall 2018
Nebraska Extension

This workbook is designed to help you through the process of communicating, understanding, and developing a sound transition plan that passes the farm or ranch to the next generation(s).

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Farm/Ranch Transition When You Aren't in Control

PRE-WORKSHOP HOMEWORK

Bethany Johnston and Jay Jenkins, Nebraska Extension Educators

Complete and bring with you to the workshop.

What do you want to see happen to the farm/ranch?

Have you been able to talk to your parents about what is happening with their estate plans? If not, why?

What is your biggest concern/anxiety/fear(s)? What are you afraid you might find out?

What is the biggest obstacle in your family dynamics?

What do you love about your family business?

What is the worse situation you can think of, which might happen in the future?

What could you learn from this workshop that would help you?

What is your *mission statement* for your farm/ranch? What is your vision for the farm/ranch?

What are your *goals* for your farm/ranch? What will you do to make your vision happen?

HOMWORK AFTER THE WORKSHOP

The To Do List

Below are five questions to ask your parents (or older generation).

Suggested wording is italicized, if you need a script. Use your own words if these seem awkward.

You need to make “notes” to yourself about the answers you received.

1. You can start the conversation something like this: *“I’m concerned about the future of our operation and would like your thoughts/answers to several questions. Please be honest. I will work very hard at simply listening.”*
 - Ask your spouse – *“What do you want to see happen to the farm/ranch?”* (Listen for their values that show up in their answers.)

 - Ask your parents – *“What do you want to see happen to the farm/ranch?”* (Listen for their values that show up in their answers.)

Note any common ground between your, your spouse’s, and your parent’s goals.

2. Ask your parents – *“I learned at a recent workshop that written documents are very important to the operation transition. Can you tell me if you have these documents in a written format, where they are located, and if you would share a copy with me?”*

“Do you have a: (Add or subtract from this list to find out about all relevant documents they may have.)

- *Written Lease*
- *Will*
- *Entity (LLC, Corporation, Trust)*
- *Buy/Sell Agreement*
- *Written plan for transfer of management and operation (land, cattle, machinery)*
- *Other*

Note:

- What does the written document look like?
- What do they have on paper and if you had to document it, could you?
- Can you have access (or copies) of the documents?

3. Ask your parents – “Another important topic covered in the workshop was health planning. While none of us like to think about things that will inevitably happen, I ask these questions with a great amount of respect.

- *Do you have Long Term Care in place to protect the farm/ranch?*
- *What does that look like?*

- *What happens if you become physically or mentally incapacitated?"*

4. Ask yourself, with input from your spouse –

- What are our unpaid contributions?
- What is the value of the unpaid contributions?
- Are my parents aware of our unpaid compensation/contributions?
- Can you explain the difference of fair versus equal in a “nice” way to your parents?

Consider that your parents and other siblings may also have contributions that they consider unpaid.

Ask your parents –

- *“I’m starting to understand that we each can contribute in different ways to the operation. Sometimes our contributions do not receive direct payment. I think it’s important that we can begin to determine what each of us contributes in ‘unpaid’ inputs.*

Can you help me write these down and put a value to the operation on each one?” (See what they come up with, they may identify contributions you’ve made that you have not considered.)

5. If the question is relevant –

- Ask your parents - *“If you intend to keep the operation in the family, I would like to be more involved with the management of the operation. What can you do to help me grow in this area?”*

- If you are a laborer, ask yourself - how could I get more management transitioned over to me?

- Ask yourself - can I explain to my parents “Passing the Farm/Ranch Business On” versus “Selling the Place & Dividing Assets?”

6. Ask your parents – *“What is your plan to share this information with the other heirs?”* If appropriate, suggest that this be done at a family meeting called for this specific purpose. Share the family meeting information on the next page, as well as the helpful resources page.

Thoughts about Having a Family meeting

Most family disputes with farm/ranch transition/succession usually go back to poor or improper communication within the family. Most could be avoided with better communications. One way to improve communication is to have a family meeting at the beginning of the process. Here are some thoughts on having this meeting:

1. Be sure that the grandparents, or the decision makers of the family are on the same page. Do they want and/or are they willing to value the input from the rest of the family? Are they ready to put together a plan for their assets? They have to agree first.
2. For the first meeting – and first meeting only – invite all adult family members to participate. Provide electronic means for those not able to attend in person. Be sure to include both on-farm and off-farm (or ranch) family members. This includes grandparents, parents, spouses, grandchildren (of adult age).
3. The purpose of this first meeting is to get input only. It needs to be tightly controlled. When giving input, there needs to be strict ground rules. Things like:
 - a. No evaluation of suggestions. Members of the family have to listen to all ideas. No one gets to criticize any idea brought forward.
 - b. When giving input, no member of the family gets to dominate the discussion. Meaning that all members are given the chance for input prior to any member giving input the second, or third time.
 - c. Take notes, record the ideas.
4. There will need to be follow-up meetings. For those decision making gatherings, the Golden Rule should apply. The Golden Rule in this case is: “Those who have the gold, make the rule.”
 - a. So the number of people at follow-up meetings will be drastically reduced. Maybe the decisions are made by Grandpa and Grandma – no one else.
 - b. Or, if decision makers include the children, the recommendation is that no spouses or grandchildren be included in the decision making portion of the discussion.
5. The vision for the transfer of the farm/ranch business or distribution of assets should be developed prior to thinking about the ‘tool’ you’d use to execute this plan. Too often families worry about the trust, LLC, or the will and confusion reigns. Have a plan**. A competent lawyer will help execute the plan with the correct tools after the plan is laid out.

****Have a Plan:**

- If the farm/ranch business is ending, then the plan consists of details about how to end the operation and how to disperse assets, to whom and when.
- If the Farm/Ranch business is continuing to another generation, then the plan will need to consider how assets are transferred. Consideration would need to be given to having appropriate income for the older generation, income for the succeeding generation, and proper consideration of the non-farm/ranch family members.
- For more information, please refer to: **Fairness in the Farm/Ranch Estate Planning** at: <https://agecon.unl.edu/succession/succession-fairness-estate-planning.pdf>

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Helpful Resources

Rural Response Hotline 1-800-464-0258

- **Farm Financial and Legal Assistance Clinics.** The Nebraska Department of Agriculture Negotiations Program, in partnership with Legal Aid of Nebraska, provides free, one-on-one, confidential finance and legal assistance for farmers and ranchers. The clinics provide an opportunity to meet with an experienced agricultural law attorney and an agricultural finance counselor. Clinics are held monthly in Norfolk, Beatrice, Grand Island, Ainsworth, Alliance, Lexington, North Platte and Valentine. To sign up for a clinic, call the Rural Response Hotline (1-800-464-0258).
- **Nebraska Counseling, Outreach, and Mental Health Therapy program (COMHT).** Legal Aid of Nebraska and the Interchurch Ministries of Nebraska (IMN) have collaborated to establish this counseling program for rural Nebraskans. Farm and ranch families and individuals of limited means may obtain no-cost vouchers to use in paying for confidential mental health counseling from participating licensed counselors. They can be reached through the Rural Response Hotline (1-800-464-0258).

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COMMUNICATION

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Seek First to Understand, Then to Be Understood

This can be very difficult to do because we assume we understand what others are saying and meaning.

Good communication can only take place in an environment of trust.

The more people understand each other, the more they trust each other.

Listening

Empathic Listening is listening with the intent to understand from the other's frame of reference. It is reflecting feelings and words back to the speaker to get clear understanding.

You should use empathic listening when emotions are high and the other person doesn't feel understood.

Empathic listening tips: focus on your intent (understanding), not the correct response. Don't be afraid of silence. If you get stuck, simply repeat their words.

Autobiographical Listening is filtering what others say through our own story, experiences, biases and values. When you listen autobiographically, you are often listening with the intent to reply. Four types: Probing, Evaluating, Advising, and Interpreting.

Clarifying Questions

A clarifying question is one that comes from the speaker's story, not your autobiography. Ask clarifying questions to move the conversation along, especially if you receive a short response from the speaker. They usually begin with "what" or "how".

Examples:

- When you say he doesn't trust you, what do you mean?
- What does it look like to make a bigger contribution to the operation?
- When you say your work assignments are demeaning, what does that mean?
- Can you help me understand what you mean when you say they are performing way below par?
- Can you tell me more?

Practice Communication

On paper, describe a situation in your farm/ranch operation that you feel strongly about and wouldn't mind sharing with the group.

Pair up with someone not familiar with your situation. Select a speaker and a listener. The speaker's job is to share the situation with the listener. Make sure you take a breath so the listener can practice good communication skills (listening and questioning). Listener's job is to understand the situation. Check your intent.

Reflect the speaker's feelings and words. Ask clarifying questions when appropriate. Check to make sure you understand what the speaker is trying to communicate. Allow some time for the speaker to provide some feedback to the listener. How did they do? What worked? What didn't?

Switch roles and repeat.

Tips for Seeking to Be Understood (once you understand the other person's perspective):

If the person you are speaking to interrupts you (possibly using their own autobiographic response), consider saying:

- Would you be willing to listen to me like I've listened to you?
- Before we go there, do you mind if I finish my thought?
- That sounds interesting. Can we come back to it later?
- I appreciate your thoughts. Will you be willing to hear me out before coming up with an answer?
- You could be right. I'd like to share my thinking without being interrupted right now. Will that work for you?

If the person you are speaking with becomes emotional, try returning to empathic listening before you continue speaking. You might also need to take a break and return to the conversation later.

If you still don't feel understood after the conversation, try following up with a written version of your point of view and possibly schedule a future time to finish the conversation.

Concluding remarks:

Know that there are some things you can influence and some things that you are concerned about that you cannot influence. Spend your time working on the things you can influence.

Consider creating a family Mission/Vision/Values Statement.

Listening

Everything in good communication hinges on listening – especially listening with the other person’s agenda in mind. You should listen for signs of life, the choices they are making, and how those choices move them toward balance or away. Listening is the gate through which all communication passes.

Empathic Listening **is** reflecting what a person feels and says in your own words. It is listening to understand. It **is not** listening to advise, counsel, reply, refute, solve, fix, change, judge, agree, disagree, question, analyze, or figure out.

There are two aspects of listening in coaching:

1. *Attention* – awareness of what we receive through our senses (hearing, seeing, and intuition). We are attentive to all the information we are receiving. We notice the breathing, the pace of delivery, the modulation of the voice. We sense the pressure behind the words – the voice may be soft or hard-edged, tentative or enraged.
2. *Impact* – what we do with our listening. What impact are we having on the other person when we listen to understand?

Three Levels of Listening

Level 1: Internal Listening

- Attention is on ourselves – on the sound of our own inner voice.
- Listening to our own thoughts, opinions, judgements, feelings and conclusions.
- Appropriate level for the other person.
- When we are in Level 1, we are unaware of the other person and unaware of our impact on them.

Level 2: Focused Listening

- Attention is a sharp focus on the other person – listening is directed at them.
- Listening for words, expression, emotion, what they don’t say, values, vision and what makes them energetic.
- Impact is on them – are they coming alive or are they becoming withdrawn?

Level 3: Global Listening

- Attention is soft focus; listening at 360 degrees.
- Awareness includes everything: What you see, hear, smell, and feel.
- Gives greater access to your intuition.
- You are aware of your impact on them.

Powerful Questions

| | Powerful | Not Powerful |
|------------------------|--|--|
| Characteristics | <ul style="list-style-type: none"> ✓ Short ✓ Simple ✓ Open-ended (how, what, who, when) ✓ Curious | <ul style="list-style-type: none"> ✓ Long ✓ Complex ✓ Multiple, serial ✓ Yes/No response ✓ Disguised solution |
| Impact | <ul style="list-style-type: none"> ✓ Client does the work ✓ Client understands bigger picture ✓ Client creates learning from their experience ✓ Client commits to action | <ul style="list-style-type: none"> ✓ Coach does the work ✓ Client gets coach's knowledge ✓ Client becomes resistant |

Sample Questions

What do you want?

What is important to you?

What will that get you?

How will you know (you have what you wanted)?

What or who can assist you?

What are some options?

What can you learn from this?

What will you do? By when?

Can you tell me more about that?

When you say _____, what do you mean?

Can you help me understand what you mean when you say _____?

Reduce or eliminate questions that begin with *would, could, did, do, don't, have* – they lead to yes/no responses. Questions that begin with “why” lead to explanations and focus on the problem.

Powerful Questions, more examples

Defining a Preferred State

1. What is it that you hope to achieve?
2. What would be your ideal scenario?
3. What would you like to see happen?
4. What would be the best situation for you?
5. What is your ultimate hope?
6. What outcome would be ideal?

Getting Focused

7. What are the ramifications of the outcome?
8. What options are available to you?
9. What is the upside of the outcome?
10. What is the downside of this outcome?
11. What is standing in your way?
12. What barriers do you have to overcome to achieve your ideal outcome?
13. What is really important to you?

Action

14. What could you do to make this happen?
15. What steps will you take?
16. What are you doing to make this happen?
17. What do you still need to do to make this happen?
18. What is your timeframe?
19. When will you do XXX?

Follow Through

20. How will you know this is working?
21. What impact will say you've been successful?

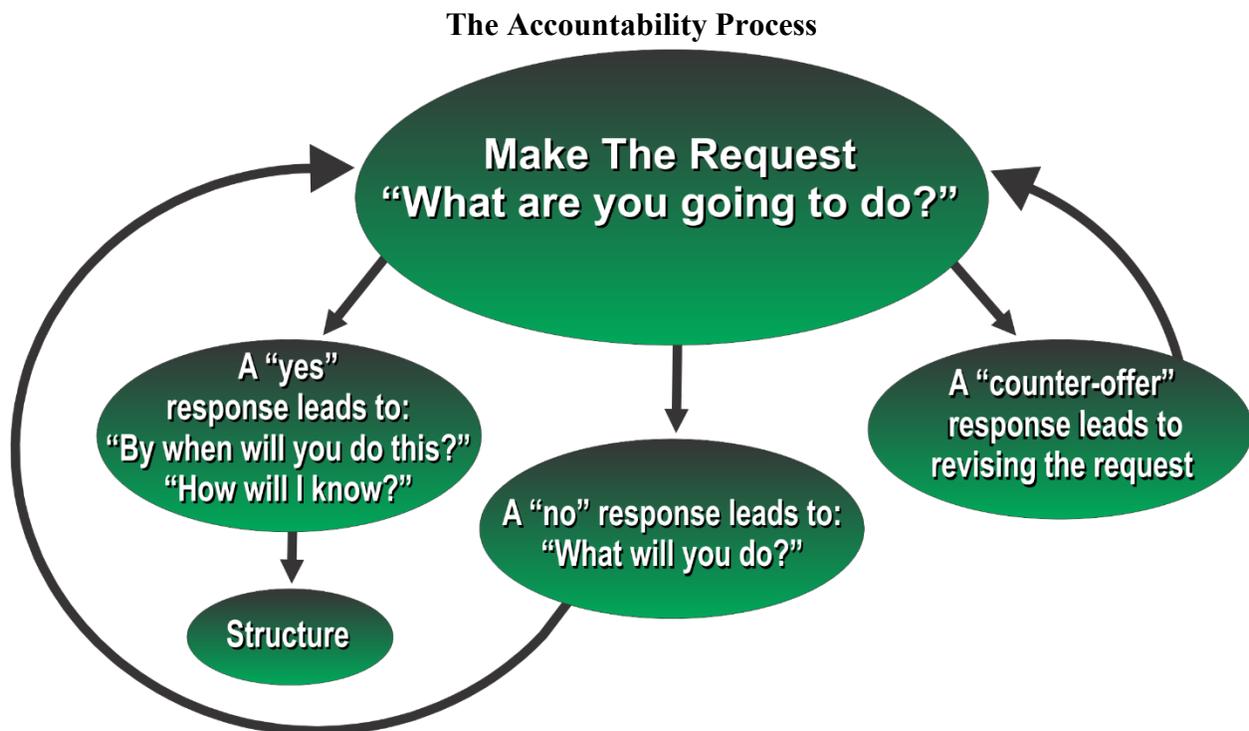
Accountability

Accountability is having the other person account for what they said they were going to do. It is determined by three questions: 1) What are you going to do? 2) By when will you do this? 3) How will I know? Accountability does not involve blame or judgment. Rather, it's an opportunity to hold them accountable to their vision or commitment and asks them to account for the results of the intended action. If need be, holding them accountable includes defining new actions to be taken.

Accountability makes the process of change more tangible, more focused, more disciplined. Consequently, the process of change is also more successful.

Together you set up the reporting process for accountability. The object is action and learning, not specific results. The person being held accountable can learn as much from failure as from accomplishment.

To be accountable means simply that: to give an account. What worked? What didn't work? What happened? What would you do differently next time?



Affirmations

Affirmations address who the person had to be in order to accomplish whatever action he or she took or awareness he or she achieved. It is the articulation of your deep knowing of the other.



| | Ignore | Recognize | Affirm |
|---------------|---|--|---|
| Focus | None | Task, goal, accomplishment | Character of the person |
| Action | None | Verbal recognition Monetary reward Memento | Verbal acknowledgement |
| Impact | Short term negative feeling, unless the work itself is primary reward | Short-term positive feeling of success | Short-term positive sense of being known as a unique individual |
| | Isolation, resentment | Diminishing return Sense of entitlement | Sustained Sense of belonging and contribution |

“I acknowledge your courage, knowing that you had difficult things to share with me today.”

“I’d like to acknowledge you for. . . .”

“I see that you are. . . .”

Speaking To Be Understood

Respectfully state your point of view using “I” messages:

- I feel ____ about ____.
- I would like to ____.
- Based on my experience, I think we should ____.
- You could be right. However I’d prefer ____.
- That sounds interesting. Can we come back to it later?
- I can see what you mean. I have a different point of view I’d like to share.
- Thank you for sharing your thoughts. Would you be willing to hear mine?

“I” messages – describe your feelings, concerns and perceptions.

“You” messages describe the other person’s behaviors and motives.

Some tips:

- If the person interrupts you -
 - Would you be willing to listen to me like I’ve listened to you?
 - Before we go there, do you mind if I finish my thought?
 - That sounds interesting. Can we come back to it later?
 - I appreciate your thoughts. Will you be willing to hear me out before coming up with an answer?
 - You could be right. I’d like to share my thinking without being interrupted right now. Will that work for you?
- If the person becomes emotional -
 - Return to Empathic Listening before you continue to speak.
 - Take a break and return to the conversation later.
- If you still don’t feel understood -
 - Follow up with a written version of your point.
 - Agree to schedule a future time to finish the conversation.

LEGAL BASICS FOR “SANDWICH” GENERATION

FARM/RANCH ESTATE PLANNING: SOME INTRODUCTORY TERMS

By Joe M. Hawbaker, Attorney at Law

This article was prepared for a series of workshops, Ranch Transition When You are Not in Control (2016), being presented by Nebraska Extension, with funding from North Central Risk Management Education. The article is not intended as a substitute for the advice of counsel. It is intended to introduce the reader to some of the basic legal issues and tools of estate planning.

Introduction

Here are the facts for our hypothetical family. Parents own most of the farm/ranch assets. They may still be involved in running the farm/ranch or they may have handed over most of the labor and management to the next generation. That generation, our “sandwich” generation, may own some assets of their own, such as livestock and equipment, and may even own some land, but the main part of the farm/ranch in our hypothetical family still belongs to Parents. In this family, there are also off-farm siblings of the Sandwich Generation. We will call them off-farm heirs.

The Sandwich Generation have committed themselves to the farm/ranch. They have been earning their livelihood at least in part from the farm/ranch, though there may be off-farm income to contribute to family living. It is likely that part of their contribution to the farm/ranch has not been compensated; their efforts in part have increased the value of the farm/ranch (built its equity) rather than come back to them in the form of salary, wages, benefits, etc. And the equity that is being built, whether sweat equity or capital improvements, may in fact belong primarily to someone else, i.e. the Parents. The fruits of the family’s labors go back into the farm/ranch – a common enough phenomenon in family agriculture.

The Sandwich Generation may also have children of their own, some of whom may be adults or approaching adulthood, and may be interested themselves in working on the farm/ranch. These are the basic facts.

In our experience, the Sandwich Generation may be susceptible to certain anxieties. The following are statements we have heard from this generation.

- Will the farm/ranch have to be sold to pay taxes at the time of the parents’ deaths?
- Will the farm/ranch have to be sold to pay the parents’ long term care costs?
- What happens when the parents die? What is in their estate plan? Will we still be able to run the farm/ranch? Will we have use of the land for our own cattle?
- We want to plan for our own retirement. What security will we have for our own retirement?
- We want to plan for our own children’s succession into the farm/ranch business.
- Will we ever come to own the farm/ranch ourselves?

- Will we have to buy out our off-farm siblings? Will we be able to do that? Will I want to take on a bunch of debt at that age?
- Will we share ownership of the farm/ranch with our siblings? Does that mean we will be in business with them? Will we have to answer to them for our business decisions or make decisions with them?
- The longer we stay out here on the farm/ranch the fewer other opportunities we will have in life.
- “Someday, son or daughter, this will all be yours” is sometimes a thin reed to lean on.
- What if the Parents become incapacitated – how will we operate and make decisions on the farm/ranch, since we don’t own it?
- What if the Parents change their mind about their estate plan?
- What if my siblings are unhappy with the Parents’ estate plan? What if they challenge that plan after the Parents are gone?

And the list might go on. In the best of family relationships, some of these concerns can arise, whether or not they are ever expressed.

So, how do we address these concerns? Communication within the family may be the most important tool. But such communication is often not easy. The Sandwich Generation may feel like they are prying, or worse, that they appear to be motivated by greed, are acting like vultures, etc. by bringing up these topics. They may feel like it is a violation of some kind of unspoken trust between parent and child to bring up these things. But communication is critical, for the relationships involved are not merely familial but business.

In our workshops we will in part air out these concerns and discuss the tools that might be used to address them. Some of these tools are legal, that is legal agreements, or structures and means of ownership. It may be helpful to have a brief background on some of the terms, concepts and tools.

Direct Ownership

Individuals, that is human beings, own the property. In using direct ownership, the question arises – how is the property to be owned? Will each person own their own separate property, e.g. a parcel to each heir? Or will the individuals own the property together, as either tenants in common or joint tenants?

Indirect Ownership

The property is owned by an entity, e.g. a limited liability company or corporation, and the individuals own the entity. Property may also be held in trust, in which individuals, as beneficiaries, own interests or shares. (In a trust, a trustee “owns” the property and manages it for the benefit of the beneficiaries.)

Joint Tenancy

A common form of ownership between spouses, where each spouse owns all of the property. Joint tenancy is characterized by the right of survivorship: last one standing gets it all. In joint tenancy, the last surviving owner determines what happens to the property after his or her death.

Tenancy in Common

Unlike joint tenancy, tenancy in common is not characterized by the right of survivorship. Each tenant in common, or co-owner, owns an undivided interest in the property, some fractional share of the undivided property. Tenancy in common provides no structure for management of

property: the co-owners need to figure out who will be responsible for managing the property, e.g. paying taxes, negotiating leases, procuring insurance, complying with FSA/USDA regulations, etc. Tenancy in common is also subject to the right of partition. (See below.)

Right of Partition

Owners of real estate, whether joint tenants or tenants in common, may in effect force the sale of property through exercise of their right of partition. This is a legal right to seek a physical division of the property in court. In that courts are often unable equally to divide property among owners, the property is sold and the proceeds divided.

Option

An option gives the holder of the option (sometimes called the optionee) a right to force the owner of property to do something with respect to that property, typically either to sell or lease the property to the option holder.¹ An option does not require that the holder of the option buy or rent the property. If, however, the option holder decides to exercise the option, i.e. decides to buy or rent the property, the option holder can compel the owner to sell or lease the property.

Preemptive Right

A preemptive right, as opposed to an option, gives the holder of the preemptive right merely an opportunity to purchase or lease the property (before it is sold or leased to a third party) should the owner decide in the first place to sell or lease. In other words, a preemptive right does not give the holder a right to *force* the owner to sell or lease property. What the preemptive right does is to limit the right of the owner to dispose freely of his or her property. Preemptive rights are also known as rights of first refusal or rights of first offer.

Closely-held Entity

A business entity, such as an LLC or corporation, for which there is no ready or available market. Often, ownership in a closely held entity is restricted to family by the entity's governing documents. For example, a closely held LLC may state in its operating or buy-sell agreement that only lineal descendants of the initial owners may ever own an interest in the company.

Buy-Sell Agreement/Provisions

This is an agreement among owners of a closely-held company that spells out what happens when one or more of the owners dies, retires, becomes incapacitated or simply wants to be bought out of the business. A buy-sell agreement places restrictions on the transfer of ownership interests by spelling out how and when and, often, for what price the transfer of ownership interests may occur. A buy-sell is something of a balancing act: how do you keep the business going, on the one hand, and, on the other, pay the departing owner a value for his or her ownership interest in the business? A buy-sell not only protects the farm/ranch (e.g. keeping outsiders from interfering in a family-run business and protecting the business from the claims of its owners' creditors, including marital property settlement claims) but creates a market for those who want or need to get out. A buy-sell may also play a role in tax planning. A buy-sell can also perform an important part in succession planning, where, for example, the buy-sell gives

¹ For our purposes we are going to assume that the option contains a right to buy a piece of property, such as part of the ranch. However, technically, an option may be for either a right to buy or a right to sell. An option which gives the holder the right to decide to buy or not to buy the subject property may be referred to as a "call." If the option gives the holder the right to decide to sell or not to sell, it is called a "put." To take it one step further, beyond which numerous complexities arise, an option which contains a combination of the rights to buy or to sell is called a "straddle."

those people who are actively engaged in running the farm/ranch the right to buy out the other non-active owners, often at a discounted price.

Life Estate Deed

Sometimes called the poor man's trust, this can be an efficient tool. The owners of property deed the property away of record (recorded at the courthouse) subject to their own lifetime right to possess and control the property. The former owners become life tenants and the new owners become what the law calls remainderpersons. The remainderpersons own the property but what they own is a future interest, an interest that is subject to the lifetime rights of the life tenant. The life tenant is entitled to possess and control the property, receive the income from it, pay the expenses on it, decide how it is managed, etc. But the life tenant has transferred the future interest to the remainderperson and so the life tenant cannot sell or encumber (mortgage) the property without the remainderperson's consent. In general, the life tenant is protected in use of the property from things that might go wrong in the remainderperson's life. The life tenancy ends automatically upon the death of the life tenant, with nothing more remaining to be done to transfer ownership to the remainderperson.

Installment Sales

An arrangement under which the owner of property sells it over time to the buyer. Installment sales can offer certain advantages, for example: 1) create an income stream for the owner (this may sometimes replace rent as a source of income for the parents in retirement); 2) begin the irrevocable transfer of ownership to the business successor; or 3) spread capital gain liability over a period of years, rather than having to pay it all in a single year. (This latter advantage may be seen by some as a disadvantage, that is, the sale triggers capital gain tax liability, whether or not it is paid over time or all at once.) There can other advantages, such as by shifting the income from the sold property to the new owner, who may be in a lower tax bracket than the initial owner, or by removing appreciation from the initial owner's estate, where the size of his or her estate creates transfer tax issues.

Care must be taken in installment sales to ensure that the sale is eligible for installment sales reporting under our tax laws. Running afoul of those rules may cause the entire gain to be taxable in the first year, while the income from the sale has been deferred over the term on the contract. There are, for example, complex related party rules that much be considered in structuring an installment sale. In general, farm machinery, equipment and livestock are not eligible for installment sales reporting – the seller must recognize the entire gain or recaptured depreciation in the first year.

Transfer Taxes

Federal taxes imposed on value of property that is transferred by gift during life (gift tax) or transferred at the time of death (estate tax). The rate for each is 40%. Most people do not need to be concerned with the federal transfer tax because of the Unified Credit, which is a credit that each citizen has to exempt the transfer of property from either gift for estate tax. The amount that can be exempted by each citizen under the credit is currently \$5.45 million. (The exemption amount was fixed at \$5 million per person in 2013 and indexed to inflation.) Spouses each have a credit which they may combine to exempt almost \$11 million of property from transfer taxes. For those people with property in excess of the exemption amount, additional transfer tax planning is advisable.

Inheritance Tax

Nebraska has an inheritance tax. Most property that a Nebraska resident owns at the time of death is subject to this tax. (Real estate in other states is not subject to the Nebraska tax.) The tax occurs at three levels: 1%, after a \$40,000 exemption per recipient; 13% with a \$15,000 exemption, and 18% with a \$10,000 exemption. The 1% tax applies for children, grandchildren, parents and siblings of the deceased. This includes spouses of those persons. The 13% applies

Basis Adjustment

Transferring assets in a *time-of-death* transfer allows the heirs (the new owners of the transferred property) to acquire a step-up in basis in the assets, and potentially to avoid capital gain taxes. Here's how it works. **Basis** is a tax term for cost and it is used to calculate capital gain. For example, if you purchased a piece of land for \$1000 an acre fifteen years ago, and that land is now worth \$3000 per acre, there is \$2000 of capital gain "built-in" to each acre of that land. If you were to sell the land, you would likely have to pay capital gain tax on that \$2000. (The maximum federal capital gain tax rate is presently 20%, to which some states will add their own capital gain tax. In Nebraska, the rate is approximately 7%. In addition, there may be imposed approximately 3% in federal tax for passive gains.) If you do not sell the land but transfer it to your heirs in a time-of-death transfer, they can receive a stepped-up basis, that is, the law will deem that they paid for the land whatever it is worth at the time of your death. (\$3000 per acre, in our example.) This happens without the payment of capital gain tax. Should the heirs then turn around and sell the land, little or no capital gains tax would have to be paid, because their basis would presumably be equal to the selling price.

Step up in basis is only available for time-of-death transfers. If property is given away during life as a gift, the donor's basis goes with the property and becomes the done/new owner's basis.

In Terrorem Clause

A clause that may be written into a Will or into a Trust, which provides for disinheritance (or a diminished inheritance) for those heirs who choose to fight about they are receiving. The clause is intended to dissuade people from contesting a Will or seeking to invalidate a Trust. Such clauses are not fool-proof; court's may still allow heirs successfully to challenge a Will or Trust; after all, what if Mom or Dad really were unduly influenced by one of the children, or truly lacked capacity to make a change to the documents later in life, etc. But such clauses can prevent heirs from raising a fuss without a real basis beyond resentment for doing so.

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CALCULATING UNPAID COMPENSATION or GROWTH IN BUSINESS EQUITY

Dave Goeller

Nebraska Extension Transition Specialist Emeritus

Nebraska Farm Hotline 1-800-464-0258

Did you influence the growth of the farm/ranch?

What is “sweat equity”?

Contribution – Compensation.....Labor vs. Management

Is an hour of Labor valued the same as an hour of Management?

Land price trends

Upkeep

Excel spreadsheet (developed by Dave Goeller & John Baker) located
at <http://go.unl.edu/FarmRanchTransition>

UNL Custom Rates

TRANSFER MANAGEMENT and RETIREMENT

Retirement- Every Day is a Sunday

Golden Rule- Fair vs. Equal

Transfer of Management

Long Term Care....costs & sources

“Around the Bend”

Dead-end situations

Financially firing on all cylinders- adding (or losing) a generation

Is step number one to set up an entity?

Exit Strategy- What if It Doesn't Work Out

Fairness in the Farm/Ranch Estate Planning Context

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Estate planning requires a careful consideration of facts and laws unique to each situation. This publication is provided for educational purposes only; it is not a substitute for consulting an attorney or other estate planning professional.

One of the most challenging issues in farm and ranch estate planning is how to treat farm heirs versus non-farm heirs. In the typical situation, one or more children come back to the farm or ranch to operate it when Mom and Dad retire. These are the on-farm heirs. The other siblings are the off-farm heirs.

Mom and Dad have two somewhat conflicting estate planning challenges: they want the family farm or ranch to continue operation in the family, and they also want to treat all their kids “fairly.” Giving equal shares of the farm/ranch to all the kids may make it difficult for the on-farm heir to continue to operate the farm or ranch. Giving the lion’s share of the estate to the on-farm heir may be (or at least seem) unfair to the off-farm kids. What to do?

There is also the challenge of the perception of differences between off-farm and on-farm sibs as to their contribution to the operation. The on-farm sib typically considers their sweat equity and contributions to management as key to the farm’s success. The off-farm sib(s) typically recognize the labor over years, but have a lower overall perceived value of the on-farm sib’s contribution.

Retired Iowa State University agricultural law professor Neil Harl has developed an approach that tries to balance the competing interests of keeping the farm or ranch operating into the next generation and treating each child more or less equally. Here is the Harl approach:

1. *Compensate the on-farm heir realistically for coming back to the farm or ranch.* Many parents under-compensate the on-farm heir (1) to reduce farm expenses and (2) with the expectation that the on-farm heir will be “caught up” when he or she inherits the farm. If the “catch-up” isn’t an explicit part of the estate plan, catching up won’t happen. Dr. Harl says “never close a year with deliberate under compensation of anyone.” The under compensation can be remedied e.g. by transferring an extra interest in the farm to the on-farm heir reflecting how much they were undercompensated that year. If this has been going on for a while, you need to be sure the books get balanced no later than when Mom and Dad retire.

Undercompensating the on-farm heir can lead to problems down the road. First, this makes it more difficult to leave enough of the farm or ranch to the on-farm heir that they can make a go of it financially when Mom and Dad are gone. Second, unless the catch-up payment is taken care of before Mom and Dad are gone, it needs to be clearly explained to the family why the on-farm heir gets more from the estate than the other kids. If it isn’t explained, the apparent unfairness can lead to family turmoil.

2. *Rent the land from the siblings.* One way to see that all the kids get something of significant financial value from the farm or ranch is to divide the farm or ranch into two parts: a “production entity” owned by Mom, Dad and the on-farm heir, and a “land owning” entity owned by the kids. The production entity would own the equipment, livestock,

buildings, etc. used to produce crops and/or livestock. The land entity would own the land. This means the operating heir would rent the land from him/herself and his/her siblings. The shares could be equal shares or the on-farm heir could have a larger share of the land owning entity. I would recommend a rent formula that gives the operating heir a good chance to keep the farm or ranch profitable if prudently operated, and that would also give the off-farm heirs an opportunity to share in the operation's profitability in good years.

One note of caution: be careful of the sweetheart deals. These deals can involve some very low values being placed on equipment, land, or leases that is typically being sold or transferred from the older to younger generation. In some cases, the values assigned are justified, and in some cases they are too good of a deal to be equitable to others in the family.

3. *Give all the kids a way to get out if they want to.* Some sort of buy-sell agreement should be part of the land-owning entity so that if off-farm kids (or the on-farm kids) want out the others will buy them out. Harl suggests a 15-20 year buy-out term to make the buy-out financially manageable for the on-farm heir (who is buying out the sibling that wants out). There are IRS rules regarding allowable interest rates and valuation methods but these can be used to develop a buy-out formula. Assuming it is important to Mom and Dad that the farm stay in the family, it is legitimate to use a formula that does not guarantee the off-farm heirs the maximum price for their share of the land. Agricultural land values fluctuate significantly, just as crop and livestock prices do, and no one is entitled to the maximum price possible.

4. *Family communication is key.* When Mom and Dad decide what they are going to do, they need to explain it to all the kids—what they are doing and why they are doing it. It may not be a happy conversation but hopefully all the kids will eventually see it as being reasonably fair in the long run.

There is no easy way to deal with the issue of fairness to children in estate planning. The Harl model is one approach, and as a minimum provides food for thought in working through this issue yourself.

Reference

Neil Harl, Fairness in estate and business planning. October 2012.
<http://www.extension.iastate.edu/agdm/articles/harl/HarlOct12.html>

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Nebraska Farm & Ranch Estate Planning Overview

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Estate planning requires a careful consideration of facts and laws unique to each situation. This publication is provided for educational purposes only; it is not a substitute for consulting an attorney or other estate planning professional.

This publication is an overview of Nebraska farm and ranch estate planning issues. It contains references to other publications that provide more details regarding specific agricultural estate planning topics.

Major farm and ranch estate planning challenges include:

1. having sufficient retirement income to fund a comfortable retirement;
2. determining whether or not the farm or ranch will continue to be operated by the next generation;
3. determining whether to leave more property to on-farm or ranch heirs to allow them to continue the operation;
4. developing an estate plan to accomplish your objectives and sharing your estate plan with your family;
5. planning to transition the farm or ranch business to the next generation;
6. planning for incapacity;
7. planning for long-term medical care;
8. planning for end of life medical decisions; and
9. planning to make your death easier for your family.

Sufficient retirement income. Your financial advisor can help you determine whether you have sufficient property (including stocks, bonds, savings, IRAs, other tangible assets) to provide for a comfortable retirement. The more property needed to provide retirement income, the less property there may be to pass on to your family members.

Continue family farm or ranch. If you have sufficient property, or other source of income, to provide for a comfortable retirement and also to pass the farm or ranch on to the next generation, you need to decide whether that is what all of you want to do as a family. This can be a challenging process—perhaps the most difficult in agricultural estate planning. If you decide not to continue the farm or ranch operation in the family, estate planning becomes much simpler.

Fair or equal inheritance. If you decide to try to continue operating the family farm or ranch into the next generation, you have to be pragmatic about how that can be reasonably accomplished without completely disinheriting the off-farm or ranch heirs. Parents may want to treat all children equally, but that may prevent continued operation of the farm or ranch into the next generation. It is certainly legitimate to give the future operating heir a larger portion of the farm or ranch, particularly if the on-farm or ranch heir has contributed to the financial success of the operation. In other words, consider equitable distribution of the assets, which may or may not be equal.

If there is sufficient property in the estate where all children do receive largely equal shares when Mom and Dad have passed, the concern regarding not treating all children the same is significantly reduced. That will not be possible for some farm or ranch families, however. One approach that allows all children to share financially in the farm or ranch's

continued operation is to have the operation rent the land from all of the kids. This way all kids would receive an annual rent payment from the operation even if their ownership shares are not equal. There is no perfect solution for this issue that will fit all families, but cracking this nut will be one of the biggest challenges in developing your estate plan.

Farm/ranch business transition. If the farm or ranch operation is going to be operated into the next generation, the on-farm or ranch heirs need to learn how to operate the farm or ranch business before Mom and Dad are gone. Otherwise when it is time for them to take over, they won't be able to hit the ground running. There needs to be a gradual process where farm or ranch management decisions are shared between Mom and Dad and the future operating child.

Planning for incapacity. As we age, we may need assistance in doing things we have always done for ourselves. We may need a family financial plan for a child to e.g. be on the checking account, know what bills to pay, etc. Get children's names on the signature card at the financial institution for both financial accounts and the safety deposit box. You can discuss with your attorney options such as powers of attorney to provide a trusted backstop should the time come when you need assistance making business, financial, and medical decisions for yourself.

Long-term medical care. For most families, financing long-term medical care is a frightening prospect. Medicaid does allow property to be transferred to family members free of Medicaid claims, but with a 36 or 60 month look-back period. Unless you are able to implement your estate plan and have sufficient financial resources to fund all your long-term health care costs, Medicaid planning will be an important part of your estate plan.

End of life medical decisions. We have the ability to formally establish what level of medical care we wish to receive in our final illness through advance health care directives. Working through these options can save loved ones from having to make health care decisions for you without knowing what you want them to do.

Letter of last instructions. One way to ease the trauma of family members at our death is to prepare a letter of last instructions to give family members the information they need to know what to do at your death. This may be on the most loving things you can do for your family, and should be part of your estate plan.

For Further Information

Dr. Marsha Goeting, Montana State University Extension has prepared an excellent series of agricultural estate planning materials, available for download at <http://www.montana.edu/estateplanning/eppublications.html>

Omaha attorney Joe Hawbaker has prepared a series of excellent articles on Nebraska farm and ranch estate planning topics, available for download at <http://farmerandrancher.org/articles/>

Sufficient retirement income. Marsha Goeting, *Annuities*.

Continue family farm or ranch. Marsha Goeting, *Estate Planning in Montana: Getting Started; Transferring Your Farm or Ranch to the Next Generation*; Joe M. Hawbaker, *The Estate Planning Questionnaire; Farm & Ranch Estate Planning: an Introduction*.

Fair or equal inheritance. Shannon Ferrell et al, *Farm Transitions*, chapter 3, available for download at <http://agecon.okstate.edu/farmtransitions/index.asp>

Farm/ranch business transition. Shannon Ferrell et al, *Farm Transitions*, chapter 3.

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Long-term medical care. Joe M. Hawbaker & Dave Goeller, *Medicaid: Planning for Long Term Care in the Farm and Ranch Context*.

End of life medical decisions. Joe M. Hawbaker, *Health Care Powers of Attorney & Living Wills: Advance Health Care Directives*.

Letter of last instructions. Marsha Goetting, *Letter of Last Instructions* and accompanying worksheet; *Who Gets Grandma's Yellow Pie Plate? Transferring Non-Titled Property; Your Important Papers: What to Keep and Where*.

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Estate Planning Glossary

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This publication is a glossary of basic estate planning terms. The glossary can help you learn about some fundamental concepts in farm and ranch estate planning, and help you communicate more effectively with your family and with your team of estate planning professionals.

Advanced health care directives: also called a “living will.” A legal document indicating whether or not e.g. you wish to receive medical care to extend your life when there is little realistic hope of recovery, etc. You can also specify the level of medical care you wish to receive during a fatal illness, such as (1) comfort medical measures only, (2) limited additional medical treatment or (3) full medical treatment.

Buy-sell agreement: commonly used in family farm or ranch corporations or limited liability companies. Allows e.g. a non-operating heir to have their ownership interest in farm or ranch business entity valued and sold to other business entity members or to outside members. Used to give heirs not involved in farm or ranch operation a method for “cashing out” their inheritance but typically on terms that would not threaten the financial stability of the farm or ranch.

Common tenancy: a common form of shared real estate ownership among family members; often used to leave land in shared ownership to children or grandchildren. Has no right of survivorship; when a common tenant dies, their share passes to their heirs, not to any surviving common tenants.

Decedent: a person who has died.

Deed: a legal document used to legally transfer title to real property (land, etc.).

Durable power of attorney: often used to deal with incapacity. A parent concerned regarding financial management of their personal property could give a relative, friend or trusted business associate a durable power of attorney to take effect when the parent chooses or when the the parent becomes incapacitated by illness, advanced age, etc.

Estate taxes (federal): federal taxes assessed when a decedent passes property on to heirs. In 2017 a single person can pass up to \$5.49 million without paying federal estate tax; a married couple can pass up to \$10.98 million without a federal estate tax. This amount is adjusted annually for inflation.

Health care power of attorney: a legal document giving a family member or other trusted person the legal authority to make health care decisions for the (often elderly) person granting the health care power of attorney.

Inherit: to receive property from a deceased person.

Intestate succession: dying owning property without a valid will. Nebraska law determines who inherits the property in the absence of a valid will; somewhat surprisingly a surviving spouse will share the property with any surviving children or with any surviving parents of the deceased. Dying intestate can be avoided by having a will prepared and/or by estate planning.

Joint tenancy: a common form of shared real estate ownership among family members, usually used by a married couple. Has the right of survivorship: when one joint tenant dies, their share automatically passes to the surviving joint tenant (or tenants).

Letter of last instructions: a letter to provide information helpful to your family in dealing with your death. Contents could include funeral wishes and directions, location of important legal and financial papers and documents, and information regarding insurance policies, safety deposit box, financial and investment accounts, etc.

Life estate: a property interest in real property where the life tenant has the right to use the property only for the period of their lifetime. At the death of the life tenant, the property passes to the remainderman.

Living will: see Advanced health care directives.

Medicaid planning: planning for how leave property to heirs without disqualifying oneself and/or one's spouse for Medicaid eligibility for long-term care assistance.

Nebraska inheritance tax: state tax paid by those who inherit property from a decedent. 1% with \$40,000 exemption for close relatives, 13% with \$15,000 exemption for other relatives, and 18% with \$10,000 exemption for non-relatives. Paid to counties.

Partition: legal right of a joint tenant or common tenant to go to court to dissolve the joint or common tenancy even if the other joint or common tenants disagree. Partition can be avoided by putting jointly owned land into a trust, etc.

Personal representative: a person named in a will or appointed by a probate judge to administer the estate of a decedent. Formerly referred to as an executor or administrator.

Portability rule: For married couples, any unused federal estate tax exempt amount remaining after the first spouse dies can be used by the surviving spouse at their death if the proper IRS forms are properly filed. Means a married couple does not need to split their estate in order to receive a double exempt amount.

Power of attorney: a written, notarized document in which one person gives another person the legal authority to conduct certain acts on his or her behalf, e.g. to make certain business, financial, or health care decisions.

Probate: process of settling the estate of the deceased. Personal representative gathers all of deceased property, pays outstanding debts and taxes, and distributes remaining property according to will or the Nebraska intestate succession statute.

Remainderman. In a life estate, the person who succeeds to the property when the life tenant dies. If Dad creates a life tenancy in Mom in his will with Son as remainderman, this mean Mom has the farm and its income as long as she lives after Dad dies. But Mom cannot sell the farm. When Mom dies the farm passes to Son.

Supplemental statement: a document referred to in a will listing who will receive specific pieces of personal property (family heirlooms, etc.). A supplemental statement can be modified without needing to modify the will.

Surviving spouse exemption: a surviving spouse is generally exempt from federal estate taxes and Nebraska inheritance taxes.

Tax-free gifts: the amount of \$14,000 (2017) that can be given each year to any individual or any number of individuals without incurring federal gift tax liability. This amount is indexed for inflation and can change annually. Joint gifts from a married couple up to \$28,000 per year are tax exempt (2017).

Trust: legal relationship where a person (the trustee) holds property put in trust by the property owner (the donor) for the benefit of a third person (the beneficiary) E.g. grandparents establish college fund for grandkids with bank trust office as trustee.

Will: legal document containing a person's wishes and directions as to the distribution of their property after their death.

Sources

Marsha Goettling, *A Glossary of Estate Planning Terms*, Montana State University Extension Service MT200202 HR (2017).

Joe M. Hawbaker & Dave Goeller, *Medicaid: Planning for Long Term Care in the Farm and Ranch Context*.

For Further Information

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