

# Planning the Future of Your Farm: A 2012 Update on Farm Transfer and Estate Planning



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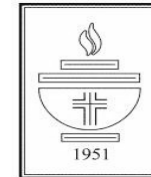


# Orientation

USDA Risk Management Agency



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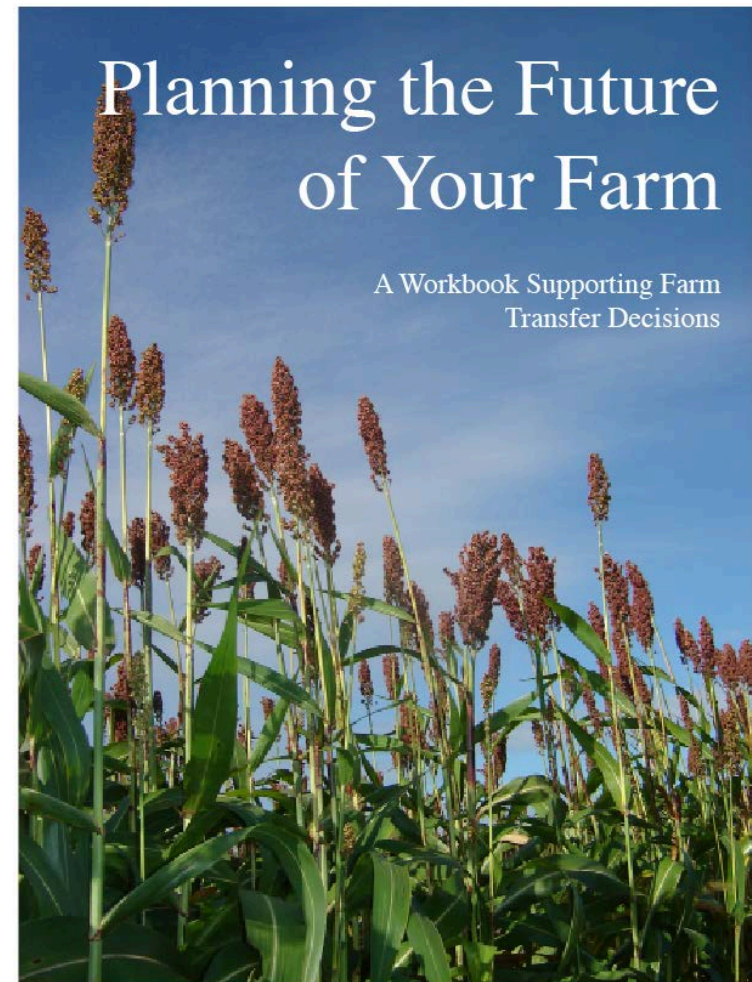
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“‘Help me’ is more  
affordable,  
than ‘Fix me’”

-Guido van der Hoeven, NCSU



# “Help Me” vs. “Fix Me”

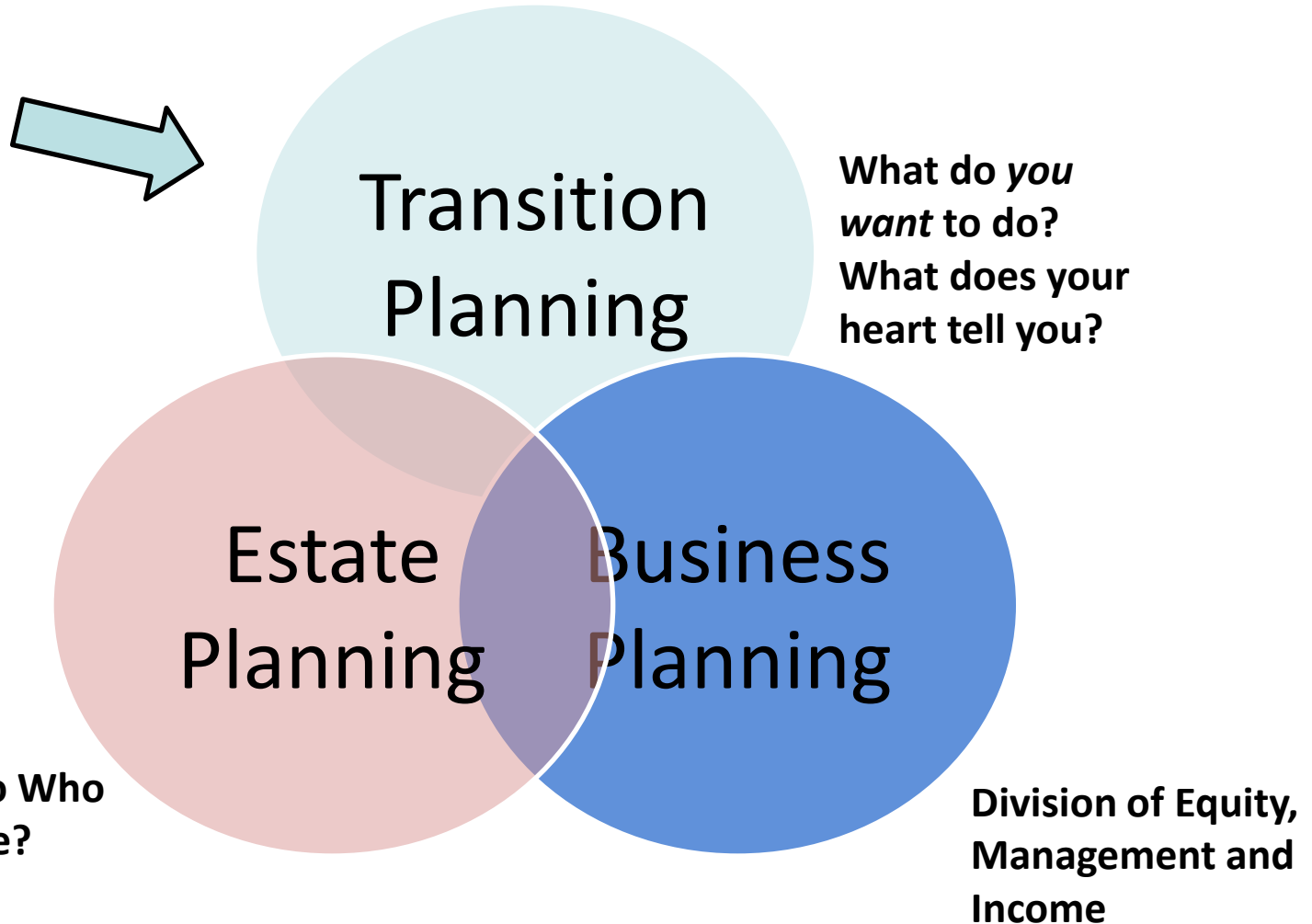
- Help Me = \$
  - Be deliberate about it
  - Educate yourself on legal issues
  - Act on that thought that is troubling you
  - Engage with professional advisers (attorney)
- Fix Me = \$\$\$\$
  - No Action or Action without Agreement
  - Less Clarity means more money to prove your interest in the subject, sort out others’ interest in the subject

# What is the compelling reason



# to *NOT* divide this up equally?

# Transfer Planning and Execution



**Farm transfer process is a fair  
allocation (by written agreement) of**

Income (and debt)  
Management  
Equity

**Fair vs. Equal**



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# Risk Management

Death □ Disaster □ Disability

Divorce □ Disagreement

Disengagement



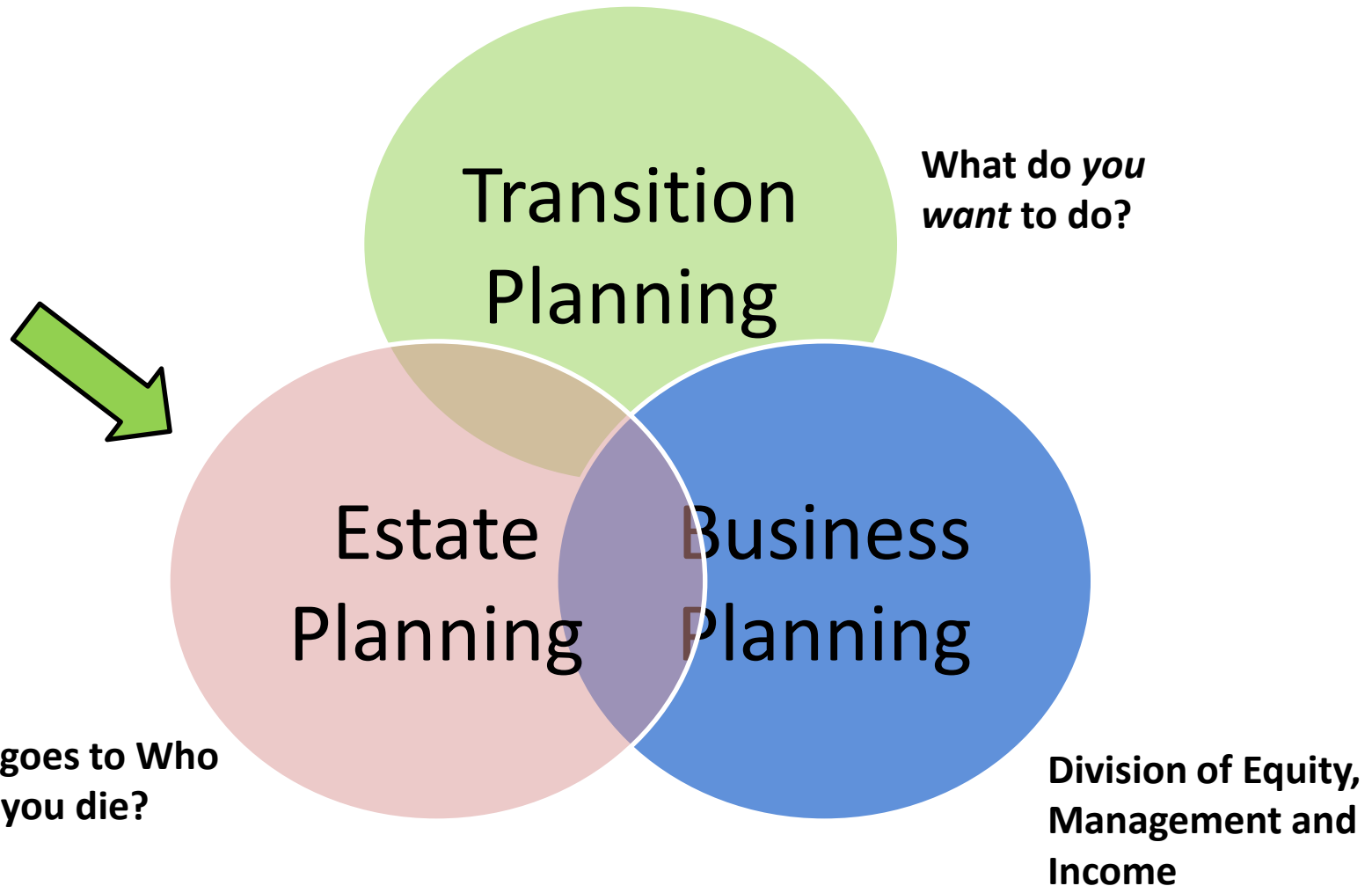


# Three questions

- What do you *want*?
  - To see happen to the farm or land
  - To do with your time as you pull back from managing farm or land
- What do you *have*?
  - Resources (financial, natural, human)
  - The law and economy as it applies to resources you control
- What do you *need*?
  - What money to live on
  - What documents to have in place for orderly distribution of management, income, control



# Transfer Planning and Execution



# Your Property

- Personal
  - Transfer on death
- Real (land and stuff attached to land)
  - Tenants-in-Common
  - Joint Tenancy
  - Tenancy by the Entireties
  - Trust/Entity
  - Remainder interest – life estate



# Your Estate

- Taxable Estate
  - All the “stuff” that you have ownership of when you die
  - Appraised at death to determine whether any estate tax is owed
- Probate Estate
  - All the stuff that does not pass by operation of law when you die (ie. trusts, joint property, insurance)
  - Managed by Executor/Personal Representative, overseen by Clerk of Court
- Augmented Estate
  - A Percentage of what you owned that you *should* have left your spouse



# Forget “Equal”

- Fairness of estate distribution is a matter of
  - Your desire to see the farmland continue to be farmed
  - Your confidence that successor will produce income from land for your ‘retirement’ support
    - Successor’s knowledge of whether will get land
  - Your farm operation’s present success i.e. your ability to *afford* estate equality with insurance



# Your Taxes

- Property Tax – how the county/city government gets revenue
  - Transfers affect qualifications for agriculture use
- Income Tax – how the commonwealth and federal governments get revenue
  - Individuals, trusts or entities earning revenue
  - Transfers affect who pays these taxes
- Estate Tax – how the ~~state and~~ federal gov't gets revenue
  - Individuals that have died
  - Exemptions = the point up to which no tax is owed



# About the estate tax...

- Exemption = \$5,120,000 per individual
  - \$10,060,000 per couple
  - Unused portion goes to surviving spouse
- Gifting = Still \$13,000 per year
  - Lifetime exemption = \$5,000,000
- Top rate = 35%
- January 1, 2013 reverts to \$1,000,000, non-portable exemption, and top rate of 55% (very large estates) (Gift remains at \$13,000)



# Gift tax in 2013...

- Currently at \$5,210,000
  - Amounts over annual exclusion in calendar year are reported to IRS
- Current annual exclusion: \$13,000
- 2013, goes up to \$14,000
- Combined gifts from husband and wife double amount
- Keep records of your gifts (have your attorney make you do it)





# Wills

- Must be properly executed (self-proving)
- Planted or Cooked?
- Executor pays debts
- Executor distributes property
- Clerk of County Court oversees process
- Suggest Guardianship for minors
- Establish trusts for minors/special needs
- Direct Assets to Credit shelter trust (manage potential estate tax)



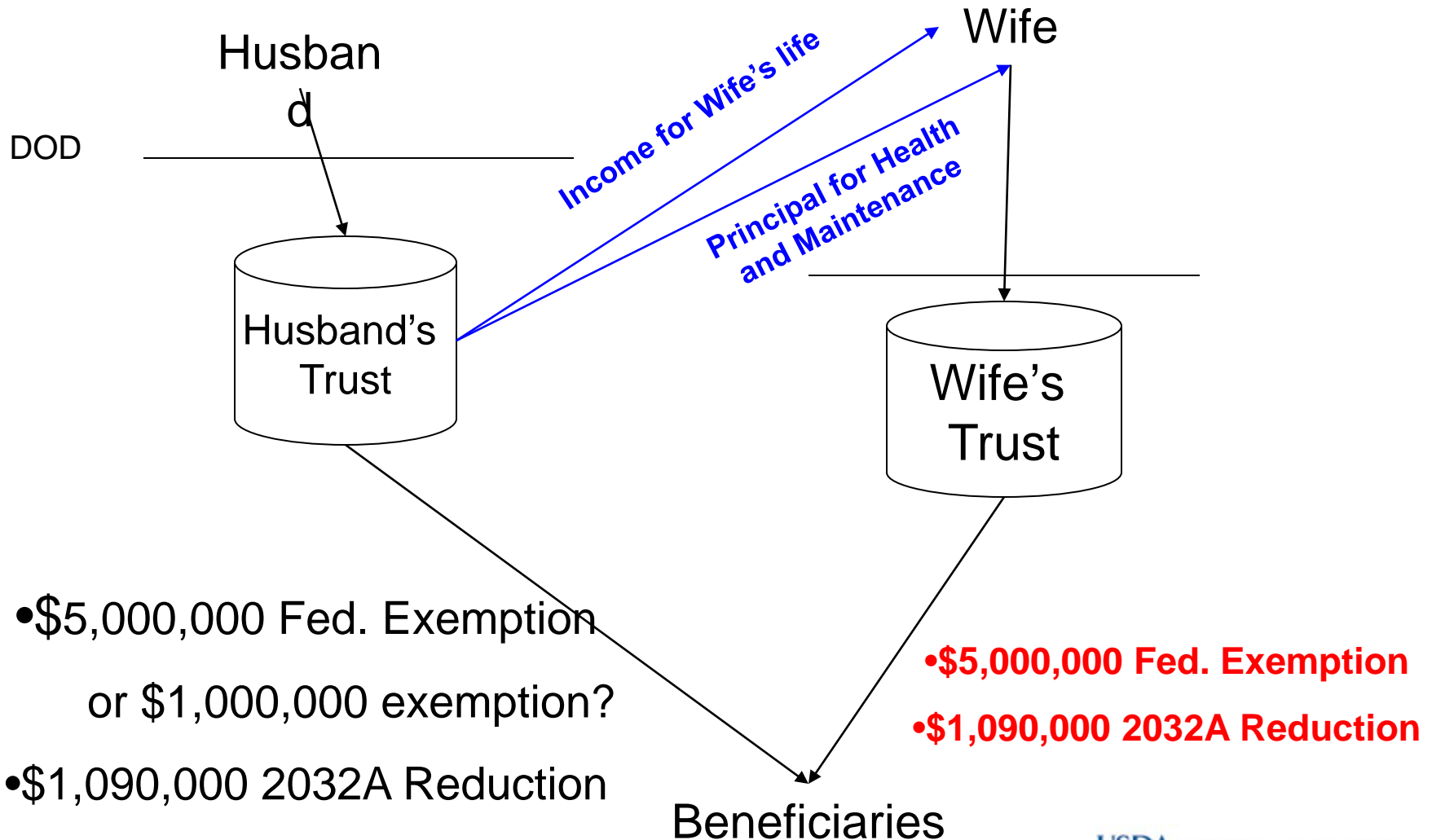
# Trusts

- Legal arrangement where one party (trustee) holds legal title of property for the benefit of another (beneficiary)
- Trust is created when another party (settlor or grantor) gives money or property to the trustee
- Intervivos or testamentary

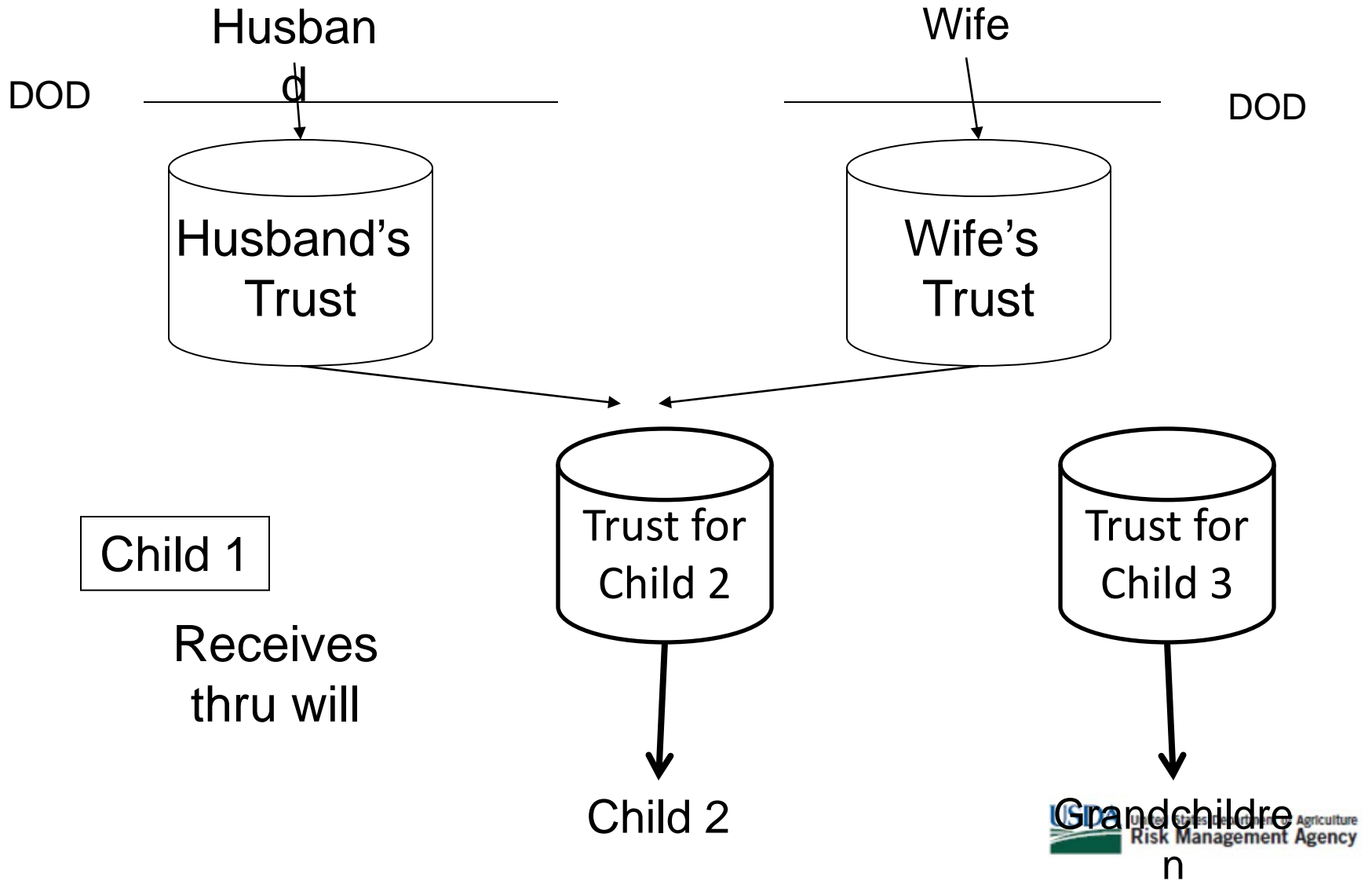
# Benefits of trusts

- Avoids probate (since probate tax is so low in North Carolina, not really a benefit)
- Private
- Can provide for individuals with special needs, persons who can't manage money, or for minors
- Allow spouse to receive income while keeping property out of spouse's estate
- Life insurance exclusion from estate (ILIT)
- Manage Farm Assets (Trustee Succession)

# Trust Based Estate Plan



# Managing Family Challenges



# Gifting of Assets

- Unconditional, no strings attached
- Sound valuation method (appraisal, assessed value)
- Carryover Basis: precludes asset getting a step up in basis through an estate
- \$13,000 annual (\$26,000 couple)
- Lifetime exemption same as (and tied to) estate tax exemption (\$5,000,000)
- Build equity in next generation
- Escape Medicaid? Provide piece of mind?

# Life Insurance

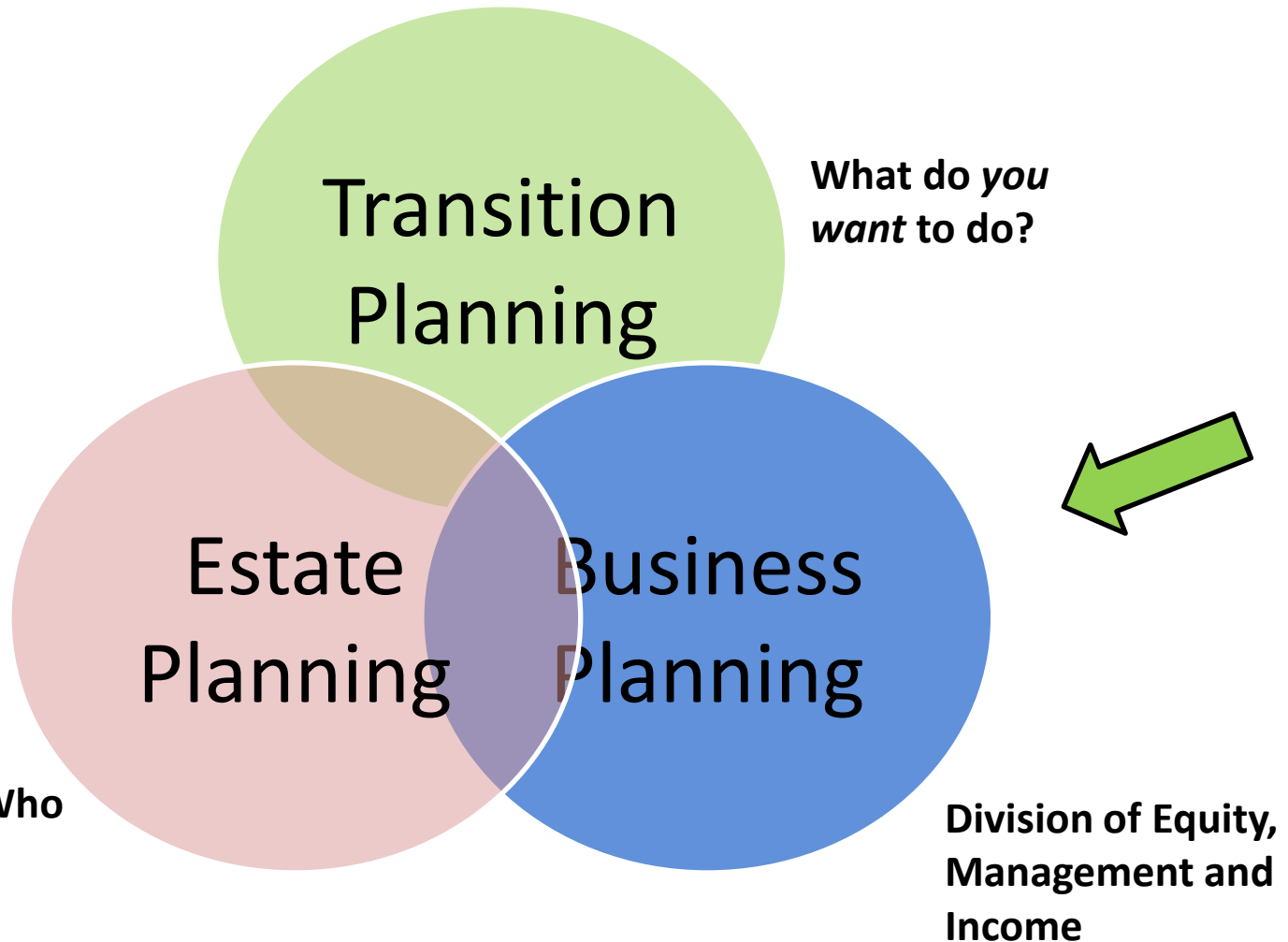
- Estate Equalization or Debt Payoff
- Payout is subject to federal estate tax if owned by insured
- Have your attorney review proposal from insurance agent (help you understand the policy's cost and health, not its promised payout)
- Irrevocable Life Insurance Trust
  - Life Insurance policy is placed in a separate irrevocable trust
  - The irrevocable trust causes the payout to not be subject to federal estate taxes
  - The premiums are gifts made to the beneficiaries

# If you *don't* die

- Power of Attorney
  - Simple (statutory form) or complex (depending on family dynamic)
  - Recorded with Register of Deeds to ensure durability
  - Can make asset transfer decisions if needed (matter of TRUST)
- Health Care Power of Attorney
  - Eliminates confusion with care providers
- Living Will (Advance Medical Directives)



# Transfer Planning and Execution



# Where Compelling Reason is Farm Succession

- Transfer of Income, Management, and Equity (if any) in production assets
- Income = business
- Long term business plan based on access to resources
- Business Continues? Business Ends? Business Begins?
- Successor is debtor; off farm heirs are creditors



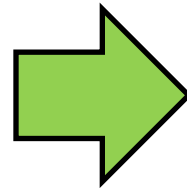
# Feasibility

- Production
  - What can farm and resources (e.g. people) produce?
- Financial
  - What is source of capital?
    - Older generation protects liquidity? Borrow on assets?
    - Younger generation borrowing capacity?
- Legal
  - Manage risk to all of above, especially family
  - Understand unintended reactions

# Use of Business Entities

- Complexity
- Business Purpose (must follow the *rules*)
- Contract between owners
  - Income
  - Management
  - Equity
- Buy-Sell (Control)
- Vehicle for reducing parents' estate value
  - Valuation discounts

Place land into LLC  
and heirs % ownership in LLC



Restricted  
Personal  
Property

- Children get % of ownership subject to transfer restrictions
  - Can receive increased ownership through annual gift
  - Transition of farming heir from “member” to “member/manager)
  - Valuation discounts?



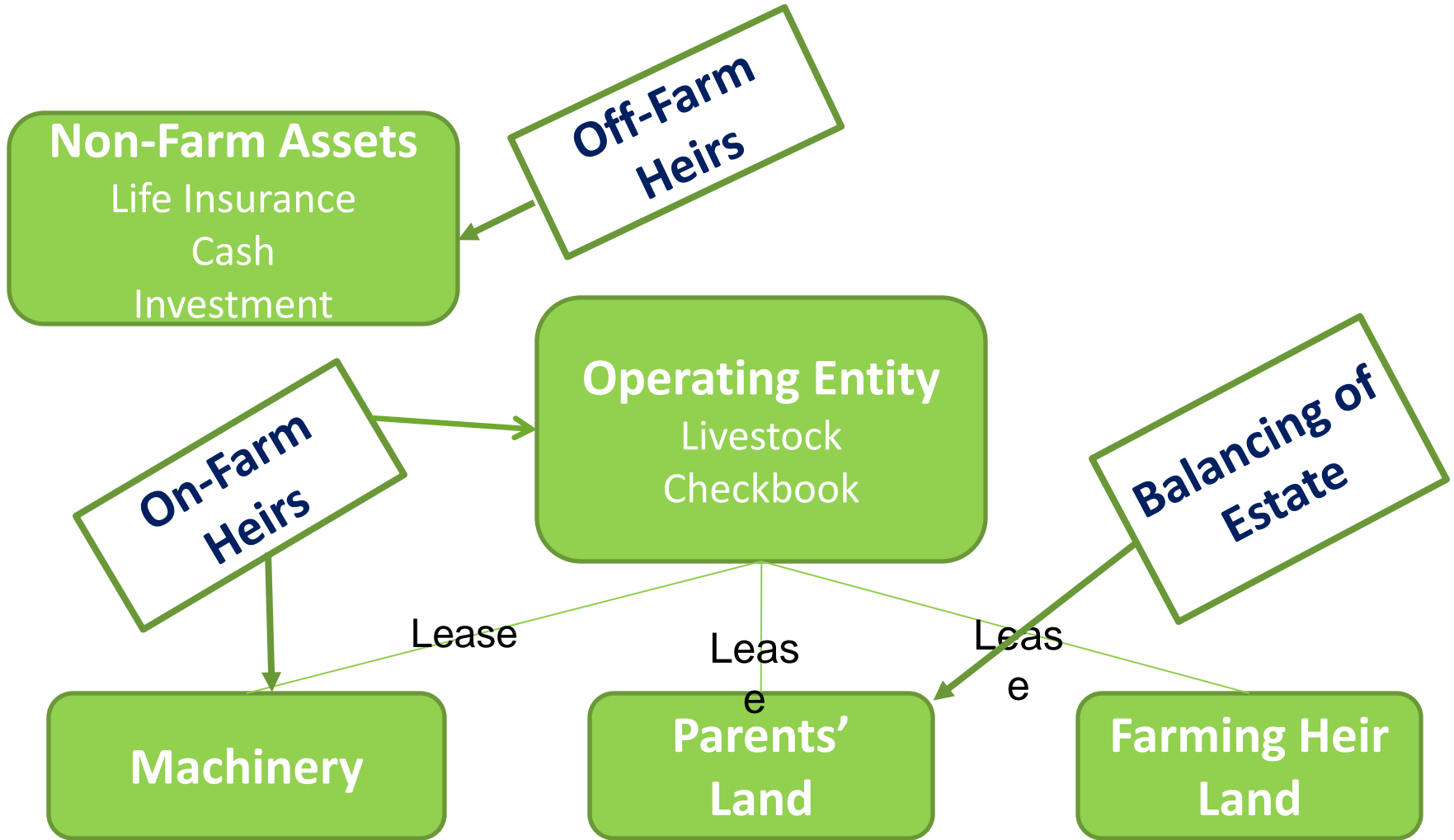
# Business Entity Documents

- Owners and Ownership
- Management Authority
- Transfer Restrictions

A contract between the owners regarding what happens when an owner wants or is forced to transfer interest



# Large Farm Transfer Plan



# The Organization Book: Demonstration of Business Purpose

- Articles
- Operating Agreement
- Resolutions/Gifts
- Ownership ledger
- Ownership Certificates (not registered as securities)
- EIN, Deeds, Leases

Know the plan, withstand outsider  
scrutiny





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LAWYER

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