

Farm Transfers in Wisconsin



a Guide for Farmers

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Introduction

Data culled from various sources show that at least 40 percent of Wisconsin's farmers are age 55 or older. The United States Department of Agriculture (USDA) estimates that over 500,000 of the nation's two million farmers will retire during the next decade and that they will be replaced by 350,000 entrants. Applying USDA's estimates to Wisconsin's farmer numbers, approximately 20,000 farmers will retire during the next decade. They will be replaced by 14,000 entrants. This means a potential for literally thousands of farm transfers in Wisconsin over the next ten years, at a time when we see complex and rapid changes in the industry due to technological innovations, trade and other government policies, a growing world population, and urban pressures on agricultural lands, as well as conservation issues and environmental concerns.

The generation of farmers approaching retirement represents a generation with fewer children and whose children have had the benefit of other life choices, perhaps more than any previous generation in history. Consequently, fewer numbers of farm families have children who want to or are able to take over the family farm. In past generations, there was nearly always someone in the family to take over the farm and carry it into the next generation. Many young couples today need to accommodate the spouse who has his/her own career to pursue, separate from the farming operation. Many young people today want to have a lifestyle as comfortable as their urban counterparts. They may be unwilling to do without now, on the gamble that the future will be better.

These changing demographics have an impact not only on the availability of young people to take over; they also mean that farmers in the older generation may put off making plans for retirement simply because that son or daughter is not there to take over the reins to the operation. Additionally, young people who may want to enter farming may not have the "farm connection." They, too, face new challenges in order to pursue their dream.

The information provided in this guide is intended to give retiring or exiting farmers and beginning or entering farmers an overview of the obstacles, the options and the opportunities available to both generations as they face farm transfers from one generation to the next. This guide does not purport to have all the answers, nor is it intended to replace the attorneys, accountants, and other professionals you will need to work with, but it should give you some basic ideas on how to analyze, plan for, and manage farm transfer issues.

Throughout the publication you will see quotations from Wisconsin farmers who have been involved in farm transfers or whose transfer is in process. Although each situation is unique, the perspectives of these farmers can provide valuable insight and wise counsel as you begin to think about and prepare for your farm transfer.

Chapter 1

Starting at the Beginning

Where Are We Now?

Whether you are planning to leave farming or thinking of getting into farming, an important first step is taking stock. Before you can decide on future plans, you need to find out where you are now. Reviewing your current financial situation accurately will help you avoid or reduce future problems. Farming is a risky business for both the buyer and the seller, and limiting the risk by sound financial management is essential. If you cannot manage the finances, the finances will manage you. Lack of money will limit the productivity and efficiency of any farm operation.

Taking stock financially for persons either entering or exiting farming involves the same process and uses the same financial tools. It is important to take an inventory of all property and possessions owned and all debts owed. An accurate assessment of debts and assets will let you know if there is enough equity available to borrow additional funds or survive tough financial situations.

Cash flow projections are an important planning tool in financial management. You need to look carefully at the operation's past years' cash income, operating expenses, debt servicing, capital replacement, and family living. The operation's past history can provide valuable data upon which to base future plans. Review your cash flow projections carefully. Make sure they are based on realistic production and price levels. Cash flow projections should provide adequate money to repay debt and replace old machinery, equipment, and buildings. After all these considerations, the operation must provide adequate cash flow for family living needs.

The Farm Balance Sheet

The balance sheet is a financial instrument that shows the financial position of a business at one point in time. It contains a list of assets and their values compared to a list of liabilities and their values, as well as an owner's equity. Assets are the items owned by the business. In a typical farm business, assets are cattle, machinery, feed, growing crops, and real estate. Liabilities are debts the business owes, such as accounts payable and short- and long-term bank notes.

Equity is the net value the owner has in the business and is calculated by subtracting total liabilities from total assets. Equity is also known as net worth.

The balance sheet always lists the assets on the left side of the balance sheet and the liabilities and net worth on the right side. Typically, the balance sheet will be broken into three sections—current, intermediate, and long term. The three sections represent the time period an asset will be held or a liability will be paid off. In a farm business, the current assets include cash, savings accounts, feed inventory, growing crops, and market livestock. Current liabilities include such things as accounts payable, rents payable, and accrued taxes. Intermediate assets can include breeding livestock and machinery, and intermediate liabilities are generally loans on these items. Long term assets are farm buildings and land, and long term liabilities are loans on buildings and real estate.

The balance sheet is an important financial analysis tool whose basic function is to show the financial viability or health of the business. A fundamental principle of financial analysis is to balance the assets with the liabilities. For example, the ratio of intermediate liabilities to total liabilities should be about the same as the ratio of intermediate assets to total assets. Another important ratio is the debt to asset ratio, which is calculated by dividing the debt by the assets. Many lenders like to see this at less than 50 percent. A 50 percent debt to asset ratio can also be explained this way: for each \$1 of assets there is \$.50 of debt. A comparison of debt to assets can be done by time period or by total debt to asset calculation. In either case, the ratio should be comparable.

Preparing the Balance Sheet

A farmer should prepare his/her own balance sheet. A critical first step in preparing a balance sheet is to determine accurate values for farm assets and liabilities. An independent appraiser should be used. It is also very important to list all debts owed accurately and completely. If the balance sheet is used in a loan application, a lender will need complete, accurate, and justifiable data. An accurate balance sheet will make the loan application process much easier. Many lenders will require an annual update of the balance sheet. An accurate initial balance sheet will make updating the data easier.

A comparison of balance sheet data from year to year can be a beneficial tool in analyzing the farm business and is essential in computing profitability of the farming enterprise. An increase in liabilities and/or a decrease in assets is an indicator of cash flow problems. A profitable business should, in a normal business year, reduce liabilities and increase assets. Most balance sheets used by farmers base the asset values on market values of the assets. Market values of livestock and feed inventories do change quite frequently. This can affect the total value of the farm assets from time to time. Machinery and equipment lose their value over the long term and should be replaced periodically to maintain the overall value. Land values, however, do not vary a great deal from year to year. Taking these factors into consideration when preparing balance sheets gives you a more accurate analysis of the farm business.

Decisions, Challenges and Conflict

The decision to sell a farm business can be very difficult and filled with a mixture of emotions for exiting farm families. Retiring farmers have frequently invested the better part of a lifetime developing a successful farming enterprise. The farm represents much more than a “business” venture to the retiring owner. Dealing with a transfer of property can be a difficult process, especially if there has been a significant personal investment in the property. This can make it much more difficult for an exiting farmer to negotiate, to measure value, and to let go, since emotions about the farm can cloud the individual’s judgment.

Entering farmers are faced with different but equally difficult decisions and challenges. Entering farmers are concerned with developing a business plan which will support their decision to purchase a farm. This focus results in a desire to negotiate the best terms possible, including the lowest price for the property. Even for individuals who have been involved in farming for years, the added responsibilities of farm ownership can be intimidating. The awareness of the increased pressure to generate income to meet expenses, to repay debts, and assume the risks involved in farming can result in added stress during the negotiation process.

It is important to recognize that the differences in perspective between exiting farm families and

entering farm families can create conflict. Additionally, within the family unit each individual will have his or her own objectives, which will differ according to the goals, attitudes, and needs of the individual. Conflict over these internal issues can be very disruptive to the family unit. You should know that although there may be conflicts between both different generations and/or members of the same generation, this is a normal and natural part of the process when families are making significant life-style changes. When viewed in a more positive light, conflict can provide an incentive for change and an opportunity for growth when it is addressed and resolved.

The objective for families experiencing such turmoil should not be to resist or avoid dealing with these differences but to resolve them by working toward mutual understanding, communication, and teamwork between the parties. Although the issues surrounding major life changes often seem larger than life itself, improving communication and negotiation skills or using mediation for particularly difficult conflicts can help farm families reach positive solutions that will benefit all parties.

Positive communication is one of the most useful tools for managing conflict. Misunderstanding, differences in perception, and differences in values all provide potential sources of conflict. Good communication involves both the ability to express differences and the ability to listen actively to other views. Working toward improving communication will enhance opportunities to reach a win-win resolution of a conflict.

Problem Solving

Learning how to define a problem and accurately describe both the problem and feelings about the problem is a skill that can be developed and improved. There are a variety of elements in the process of communication. Each must be dealt with to maximize the effectiveness of communication. Some of the key elements of good communication are as follows:

- Be prepared. Take time to set forth for yourself what you believe to be your rights in the conflict, determine your ideal solution, determine what you actually need to resolve the problem, and identify your feelings both about the problem and the possible options for resolution.

- Talk directly to the other person and express the problem and proposed options for resolution in terms of your own attitudes or perceptions, not in a critical or accusing manner. This can be accomplished through the use of “I” messages. For example, “I feel hurt when decisions are made without talking to me because it makes me feel that my opinions aren’t important” may be received more positively than “You hurt my feelings when you make decisions without talking with me first.”
- Blaming or putting down the person your conflict is with can create a defensive, resistant, and hostile environment which is counterproductive to conflict resolution. Trying to put yourself in the other person’s shoes can help you develop an understanding of their point of view.
- If a particular situation is very difficult to deal with or very emotional, it can help to state this at the beginning. It doesn’t mean you need to apologize for your feelings; however, it may help the other person understand what you are feeling if you acknowledge that the discussion is uncomfortable or stressful for you. Expressing your emotions honestly can reduce negative tensions and provide a better environment to work on problem resolution.
- It’s okay to take time to think before you talk or respond to something someone else has said. Make sure that you are prepared to discuss the problem and your feelings by setting up a convenient time and place in advance.
- Don’t assume that you know what the other person’s perceptions, rights, wants, needs, or values are. Making assumptions about what another person thinks or feels can create an environment that does not encourage parties to be open and cooperative in developing options for resolving conflict.
- Show respect for the other person’s point of view by allowing him/her to speak without interruption.
- Show that you are paying attention to what the other person has to say. To do this, you need to stay focused on the other person and maintain appropriate eye contact while the person is talking. Looking away, showing boredom with what the other side is saying, having side conversations, or fidgeting are all ways of showing disinterest in what the other person has to say.
- If you are not clear about something the other person has said, ask questions to clarify your concerns.
- Summarize the key points that you heard the other person present.
- Acknowledge the value of issues and feelings that have been expressed. This does not mean that you need to change your own values or feelings; only that you acknowledge the validity of those expressed by another person.

Calling on the Experts

Communication skills can be improved through practice. Sometimes, even if the parties are using good communication skills, conflict may escalate to the point that the parties cannot resolve their differences alone. If you are involved in such a conflict, the process of mediation can be a useful tool for parties to find a way to resolve a conflict in a manner which is beneficial for all parties.

What is mediation? It is a voluntary process in which a trained person, referred to as the mediator, assists individuals by providing a “safe” environment to discuss problems and potential options available to resolve those problems. The mediator has no authority to make decisions for the parties in a mediation, but is responsible for controlling a process designed to assist the parties in resolving their dispute.

A mediator is not an advocate for one party or the other. A mediator is not an advocate for one possible solution over another. A mediator is a trained professional who remains neutral or impartial during mediation.

The goal of mediation is to allow the parties to reach a mutually agreeable settlement. Mediation allows everyone involved to have a part in solving the problem. Mediation can promote better communication and it provides

the parties with an opportunity to participate in making decisions that often significantly affect their lives.

Mediation sessions are held in a setting that is as neutral as possible for all parties.

The mediator controls the process by enforcing a set of ground rules, including specific stages through which mediation proceeds. These rules are designed to provide each party with a balanced opportunity to participate in problem-solving.

The first stage of mediation provides each party with an opportunity to present an opening statement to explain the problem from his or her perspective. Each party is allowed an opportunity to make this statement without interruptions by other parties.

After each party has had an opportunity to make an opening statement, the mediator will allow parties an opportunity to express feelings that may be obstructing communication and blocking a resolution. This stage is called ventilation. The mediator's role during this part of the process is to ensure that parties do not make personal attacks on each other or become belligerent, while allowing for the expression of feelings.

After these initial stages the mediator assists the parties in identifying and clarifying the problems to be dealt with in mediation. The mediator will help the parties redefine and restate the issues in a non-competitive, non-adversarial way to make the problem a joint problem.

After the issues have been defined, the mediator will assist the parties in working toward resolution of the issues. The mediator will help identify issues that the parties may be able to resolve more easily. Sometimes reaching agreement on smaller issues can encourage parties to work together on the more difficult issues.

The mediator helps the parties identify potential options for resolving issues, assists parties in analyzing the strengths and weaknesses of the options, and facilitates negotiations by keeping communication open and keeping the parties focused appropriately.

Mediation may be completed in one session or it may take multiple sessions if there are many issues or very difficult ones to be resolved. Negotiation between the parties may involve

face-to-face negotiations in a joint session or may involve the use of a separate caucus, where parties are physically separated and the mediator goes between the parties. Mediation may be done in person or by telephone.

The final stage in the mediation process is preparing a written document to confirm the details of the agreement. All parties are asked to review and approve the written agreement. Once this has been done, the agreement becomes a binding contract between the parties.

The mediation process encourages the development of trust and cooperation by maintaining a safe, respectful environment for parties to work toward meeting their individual needs or goals in a manner that is confidential, informal, cost effective, and flexible, and can be beneficial for improving both the business and personal relationships between the parties involved.

Sample Balance Sheet and Cash Flow Worksheets

Balance Sheet								
Name: <i>SAMPLE</i>				Date: <i>10/21/2004</i>				
Current Assets	Units	\$/Unit	\$ Value	Current Liabilities	% INT	Payment	\$ Owed	
Cash				Income Tax				
Savings			1,000	Taxes (Real Estate)				
Account Receivable				Taxes (Other)				
Feed				Feed Mill	0.00%	1,150	1,150	
Corn	9,500	1.75	16,625	Oil Company	0.00%	750	750	
Oats	1,500	1.50	2,250	Vet Bill	18.00%	3,009	2,550	
Hay	53	65.00	3,445	Farm Plan	18.00%	1,770	1,500	
Corn Silage	645	20.00	12,900					
Haylage	400	47.50	19,000					
Steers	10	350.00	3,500					
Life Ins. Cash Val			0					
Stocks and Bonds				Loans on Life Ins.				
Other _____				All Other Cur. Debt – Non Farm Debts			2,460	
Total Current Assets			58,720	Total Current Liabilities			8,410	
Intermediate Assets				Intermediate Liabilities (1 to 10 years)				
Trucks & Vehicles				Notes Payable	Yrs.	%	Pmt./Yr.	\$Owed
Machinery & Equipment			102,600	Bank	7	8.50	32,041	164,000
Breeding Livestock	Units	\$/Unit	\$ Value	Bank	10	8.50	8,535	56,000
Cows	118	1,100	129,800	Bank-Oper Loan	1	8.50	15,190	14,000
Bred Heifers	32	1,000	32,000				0	
Open Heifers	30	700	21,000				0	
Calves	35	300	10,500				0	
			0				0	
			0				0	
Cash Val Life Ins							0	
Coop Stock							0	
Other- Non Farm Assets			40,000				0	
Total Intermediate Assets			335,900	Total Intermediate Liabilities			234,00	
Long Term Assets				Long Term Liabilities (10 or more years)				
	Acres	Taxes	Market Val.	Farm Mortgs.	Yr	% Int	Pmt./Yr.	\$ Owed
Farm Land	204	4,500	425,000	Bank	20	8.50%	13,964	132,150
Farm Land								
Farm Land								
Residence								
Household Impv.								
Land Contr. Receiv.								
Retirement								
Total Long Term Assets			425,000	Total Long Term Liabilities			132,15	
Total Assets			819,620	Total Liabilities			374,56	
NET WORTH (Total Assets - Total Liabilities)						445,06		

Sample Cash Flow Worksheet					
<i>Cash Flow Worksheet</i>			<i>Typical Year</i>		
Crop Prod. & Sales	Acres	Prod/Acre	Units Sold	\$/Unit	\$ Sales
Corn Silage	50	15	0	2.00	0
Soybeans			0	5.00	0
Hay	125	3.5	0		0
Other					
Gov. Payments					3,400
(A) Total Crop Sales	175				3,400
Livestock Production &	Units	Prod/Unit	Units Sold	\$/Unit	\$ Sales
Milk Sales	104	170	17680	13.50	238,680
Cull Cows	20	1200	24000	0.34	8,160
Bred Heifers	10	1	10	1200.00	12,000
Calves	35	1	35	90.00	3,150
Other Farm Inc.			0		4,200
(B) Total Livestock Income					266,190
(C) Total Farm Income(A+B)					269,590
Cash Operating Expenses	Cost /Cow	% of Gross	\$/Cwt Equiv.	\$ Planned	
Car & Truck Exp.	43.27	1.6%	0.22	4,500	
Chemicals	24.04	0.9%	0.12	2,500	
Conservation Exp.	0.00	0.0%	0.00	0	
Custom Hire	48.08	1.8%	0.25	5,000	
Feed Purchased	390.81	14.9%	2.00	40,644	
Fertilizer & Lime	28.85	1.1%	0.15	3,000	
Freight & Trucking	30.77	1.2%	0.16	3,200	
Gas, Fuel & Oil	33.65	1.3%	0.17	3,500	
Insurance	29.09	1.1%	0.15	3,025	
Labor/Benefits/Pension	96.15	3.7%	0.49	10,000	
Rent & Lease	50.96	1.9%	0.26	5,300	
Repairs & Maintenance	72.12	2.7%	0.37	7,500	
Seeds & Plants	34.62	1.3%	0.18	3,600	
Supplies	96.15	3.7%	0.49	10,000	
Taxes	38.46	1.5%	0.20	4,000	
Utilities	71.63	2.7%	0.37	7,450	
Veterinarian Breeding & Medication	79.33	3.0%	0.41	8,250	
Other / Marketing	133.65	5.1%	0.69	13,900	
Custom Heifer Exp.	300.00	11.4%	1.54	31,200	
(D) Total Cash Operating Exp	1601.63	60.9%	8.22	166,569	
Net Cash Farm Income(C-D)					99,621
-Capital Purchases					5,200
+Capital Sales(Not Incl. Culls)					0
+Non-Farm Income					0
+New Loans And Other Credit					12,000
-Family Living Expenses					20,000
=Balance Avail. To Service Debt					90,521
-Present Debt Pymts & Cur. Debt					78,140
=Balance Avail. After Debt Service					12,381

Chapter 2

Farm Family

Issues and Considerations

Transfer of the family farm includes major decisions involving career choices, lifestyle changes, retirement considerations, and assumption of debt. This chapter assumes that the farm transfer will take place between two families, related or unrelated, and that their business relationship will continue over an extended time period.

Before any decisions are made about financial or legal agreements, each family should give careful thought to their own wants and needs. If the financial and legal arrangements don't meet family needs, there may be a number of very unhappy people. Each family should spend time thinking and talking about what's important to them. Then, the two families need to get together for open discussion about how each family's needs can be met. If the family farm transfer is an intergenerational transfer, from mom and dad to one or more of their children, there should be several family meetings with both generations coming together to discuss issues of concern. While family meetings can be initiated by mom and dad or by the younger generation, the younger generation may appreciate it if the parents take the lead. What is critical, however, is that the two generations get together to talk openly and honestly about their wants, needs, and goals for the future. Let's take a closer look at several of these issues.

Needs of Retiring Farmers

A farmer in Waukesha County once commented that "This farm is my day-to-day income as well as my Social Security, IRA, and retirement pension." In one sentence, he captured the dilemma of many older or retiring farmers: the farm is not just their current source of income—it is their security for the future as well. Their main concern may be that of retiring with dignity while passing the legacy of farming on to the next generation.

Retiring with dignity may mean that older farmers want a large cash settlement for investment purposes in order to live off the

farm life

Hammy still does a majority of the field work. We knew we would have to help them some. Besides, Hammy feels he has to be doing something, unless he's sick. But he's happier if he's down at the farm working.

Delores Brey

I stay out of the barn now; he does a real good job. I did milk for them when they took a weekend off here a few weeks back. I also haul manure every four days. In the last year of working together, I let him manage cows, and I did the field work (and I still do some field work). We hire out the corn planting at \$9 an acre. Hell, that's only \$900 a year, and the interest alone on the money you'd borrow to plant your own corn crop would be higher than that.

Harlan Prestein

farm life

We wanted to stay here on the farm rather than move to town right away, partly to keep an eye on things, and just because we weren't ready for town. We'll stay at least until the cows and machinery are paid off. I suppose we'd move to an apartment. It'll be great. No lawn to mow.

Norma Prestein

interest income. It may mean that they want a steady income from a land contract arrangement with the younger farmer(s) or it may mean that they are more interested in continuing to live on the farm and thus will seek a lower cash settlement or a lower monthly income to supplement the benefit of on-farm living.

Retiring farmers may also be concerned that the farm stay in the family or that the farm continue as an operating farm. They may wish to stay physically involved in the farm operation. Or they may wish to stay financially involved in the operation. In any case, they should be careful not to hamstring the work and the decisions of the younger generation.

One of the trickiest issues for retiring farm families with children is that of dividing property among their children. Some feel the property must be divided **equally** while others are more concerned that the property or estate be divided **fairly**. A fair division of property may rest more on the time or money that each child has invested in the farming operation . . . and some may have invested considerably more than others.

It's important that the retiring family think through their wants and needs. It's also important that they establish goals so their needs for financial security will be addressed in the short- and long-term future. Talking with other retired farmers can be helpful in deciding what arrangement might work out the best. Talk with several older farmers: ask them what kind of transition they used, how it worked for them, how it worked for the younger family (or families), and what they would do different if they were to do it all over again. There is a great deal of experience in your community. Tap into it. Ask questions and learn from the farm families that have gone before you.

Needs of Younger Farmers

Economic security is not just a need with retiring farmers. Younger farmers are increasingly seeking some assurance that there will be adequate money to support living expenses on a day-to-day basis. And, increasingly, younger farmers are seeking some of the things previous generations did not have: time off to get away from the farm

and money for vacations, fun activities, and home improvements.

The older generation may have taken great pride in “not being off the farm in 30 years” or in “plowing all our profits back into the farm.” The younger generation may, on the other hand, feel that it’s important to live life now; that it’s simply not acceptable to delay vacations, fun activities, or home improvements until the retirement years. Increasingly, spouse’s and children’s needs are being considered and, increasingly, spouses are from nonfarm families and don’t support the concept of delaying gratification until retirement.

It’s important that young farmers think through their wants, needs, and goals for the short and long range future. What are your monthly needs for family income right now? Will these needs change as your family increases in size or as your children get older? Are you willing to make some sacrifices now for income or security that will accrue over time? Is the farm you are considering economically viable—can it produce the income you need to cover farm expenses, meet your current needs for family income, and allow you to meet the evolving needs of the farm and family?

While it’s impossible to answer this last question with any certainty—weather, commodity prices, expenses, and other variables make it difficult to make predictions—it’s important that you calculate a worst-case scenario as well as a best-case scenario. In other words, calculate whether you would be able to make ends meet if all conditions were favorable **and** if all conditions were unfavorable. Make sure you don’t make your decision on the basis of a best-case scenario or all-conditions-favorable calculation. Farming is simply not likely to produce such conditions.

A real consideration for young farmers is debt load. Seek advice from knowledgeable people about the level of debt load that can be managed. While you may prefer purchasing the farm as well as cattle and/or machinery, it may make more sense to ease your way into farm ownership: purchasing the cattle and machinery first, **then** purchasing the

farm life

Our banker suggested that we try Daryl out for a couple of years before we make any final decisions. We also spoke with a tax man and a lawyer about what kind of agreement to draw up. They all advised us about things to watch out for. We finally agreed that I would give him a percentage of the milk check and a heifer calf each month of those first two years he was with us so he could build up some equity.

Harlan Prestein

farm life

Plan for that first month of takeover. Have \$4,000-\$5,000 put away. That first milk check doesn't come for a whole month! Certain bills need to be paid before that. Not to mention the unexpected. And some of those unexpected, the services have to be paid cash, no charging. It's scary having all those bills coming in and no check until the following 5th. And that first check is smaller than you think. It gets better — hang in there!

Bev Brey

farm once your debt load is down to a manageable size.

If the older farm family you are working with is interested in easing their way out of farming, they may be delighted to transfer ownership of the cattle and/or machinery first and then transfer land ownership at a later date.

Some younger farmers have strong feelings about using sustainable farming methods. As one young farmer in Sauk County stated “When my wife and I bought this farm, we decided we wanted to be able to drink the water when the farm was paid off.” This farmer has dramatically reduced chemical inputs and, while he is now certified as an organic milk producer, he has consistently netted profits and won awards for corn production through carefully managed farming practices. Young farmers need to be clear about whether they want to **maximize production** or **maximize profits** and they should give thought to whether sustainable farming practices can be consistent with their overall goal. If the young farmer's desire is to use sustainable low input methods, however, will the retiring farmers be in agreement? Or will they want some management control over production?

Playing It Safe

Another consideration for young farmers is the safety of the farmstead and farm machinery. Higher levels of farm technology mean that increasingly farmers and their wives and children are at risk for farm accidents. A safety audit of the farmstead and machinery might be one of the most important actions taken by a young farmer before purchasing a farmstead or set of machinery. Then, of course, it's just as important to maintain the safety of the farm over time—making repairs when needed, keeping safety shields in place —and teaching family members how to use equipment in a safe manner.

Lifestyle Philosophies and Choices

As the previous two sections point out, farm families can have very different philosophies of farming. And these can translate into different choices, goals, and needs. Quite often these philosophies, choices, goals, and

needs have not been thought through or discussed with others—frequently other family members aren't even aware that choices and goals are being made.

This unit includes several tools that can be helpful in making choices and setting goals, and in discussing these with other family members. Two of the tools are surveys (one for retiring farmers, one for younger farmers); the third is a goal-setting tool which can be helpful in identifying goals as well as action steps to reach your goals; the fourth is a tool for discussing wants and hopes in intergenerational farm transfers.

Retiring farmers are urged to do the survey entitled ***Lifestyle Values and Choices: A Survey for Retiring Farmers***, and younger farmers are urged to use the survey ***Lifestyle Values and Choices: A Survey for Younger Farmers***. Spouses could do the surveys separately and then discuss the results with their partners. Or, spouses could do the survey as a couple, discussing each item and agreeing on a response before moving on to the next item. Either way, what is important is that you take the time to be clear about your values, wants, and needs and that you take the time to discuss these issues with your spouse.

Goal Setting and Action Planning

Once you have a clear idea of what your values, wants, and needs are, you can move forward in setting goals and laying out action steps for reaching these goals. The tool entitled ***Goal Setting/Action Planning*** can be useful in creating a strategy for your future. Five things are important in the process of identifying goals and action steps:

- Have a clearly defined goal.
- Set a target date for reaching this goal.
- Identify clear-cut action steps.
- Lay out a target date for each action.
- Specify who is responsible for each action step.

Having a clearly defined goal and a target date for reaching the goal is crucial. For retiring farmers the goal may be simple and straight-forward: “To sell the farm, cattle and machinery by January 1, 200__.” If the

transition is to be more gradual or if it involves family members, the goal may be a bit more complex: “To transfer the cattle and machinery to our two sons by January 1, 200__ and to transfer the farm to our sons through land contract by January 1, 200__.” The goal for younger farmers may be simple or complex. But regardless of whether it is for younger or retiring farmers—and whether it is simple or complex—the goal should be clearly defined and it should have a target date for completion. When there is no target date or when the goal is vague, the farm family transfer may never occur or it may drag on and on, creating intense frustration for one or both parties.

Once the goal and target date have been established, it's important to identify action steps which will help you reach the goal by that target date. The action steps should also be clearly defined (or specific). They should also have target dates and should have someone responsible for accomplishing them. These three steps are the keys to actually accomplishing the goal, so be intentional about it.

Jot down every action that will be needed to reach your goal, then list them in sequential order on the goal setting/action planning sheet. Now, add target dates and list who will be responsible for doing each task. Young farmers seeking to purchase a farm might find that the following action steps would be important:

- Explore legal issues with your attorney.
- Work with a financial advisor to develop a cash flow statement.
- Meet with a lender to explore financing options.
- Do environmental and safety audits of the farm.
- Meet with the retiring family to explore a gradual transition of the farm.

While the husband and wife may be involved with each of these tasks, it might make more sense if the husband assumed responsibility for some tasks and the wife assumed responsibility for others. Of course, some of these tasks require that other people also be involved: attorney, financial adviser, lender,

We can communicate, the two of us. It's really helped to have her knowledge. I can't imagine having to buy a farm cold. I really appreciate my in-laws; they're a wealth of knowledge. More people should realize this. They have been very willing to help me, their knowledge, their just being there.

Bev Brey

retiring farm family. Make sure you outline a target date and identify who is responsible for each task on your goal setting/action planning sheet.

This is your action plan for achieving your goal. As you develop the plan or as you begin to act, you may find that the initial goal or target date was unrealistic. If this is the case, change the goal and/or the target date. Then continue to move ahead with the plan—it is your road map for the future.

Family Meetings: Communicating Hopes and Desires

Once you have given some thought to your lifestyle choices and your goals, you need to be intentional about communicating these choices and goals to others. Too often, it's the lack of communication which scuttles an effective farm family transfer: the legal arrangements may be sound and the cash flow may have been worked out to everyone's satisfaction, but **if the communication isn't honest, direct, and clear, the transfer process may literally fall apart.** This is where family meetings become so important.

Family meetings are important for the on-going operation of the farm, since they allow the family to do several things:

- Create an open, trusting environment.
- Establish goals.
- Solve problems.
- Delegate responsibilities.
- Share financial information.
- Change legal agreements.
- Air grievances.
- Share long-range hopes.
- Keep communication flowing.

Family meetings become even more important during farm transfers since the transaction will establish the course of events for years to come and anxiety levels may be higher than normal.

Regardless of whether this is an inter-generations farm transfer or a transfer between unrelated parties, it's important that the older and the younger generation meet to share their values, hopes, and goals. It's

helpful if this can be done over several meetings and if it can be structured in some way. One way to structure the meetings is to have each generation share the results of their **Lifestyle Values and Choices** exercise and to talk about differences and similarities. Once there is a trusting relationship and the two parties understand each other, they could then discuss the results of their **Goal Setting/Action Planning** exercise.

If their goals are fairly compatible, they could then enter **a joint process** of goal setting and action planning to arrive at a plan which will work for both parties. If their goals appear to be incompatible, they have two choices:

- 1) continue talking to see if they can arrive at a plan which will work for both parties, or
- 2) agree that this farm transfer probably won't work and decide to pursue the transfer with another party. A word of caution: if the goals of the two parties are clearly incompatible, it's better to admit that the transfer won't work than to try forcing a farm transfer that will create problems in the future.

If this is an intergenerational farm transfer, another way to structure the family meetings is to utilize the exercise entitled **My Wants, Hopes, and Wishes for Our Farm Operation**. All people involved in the transfer can come together and each individual is asked to jot down his or her responses to the issues outlined on the exercise. Then each person shares his or her responses to each question with other family members. It's important that **each person**—husband **and** wife, older **and** younger generation—speak up. If the hopes and wishes of the parties are at first incompatible, it's important to talk further to see if you can arrive at an arrangement that will be workable to everyone involved. Again, it's better to recognize that a potential transfer won't work than to enter into an agreement that is doomed for failure.

It should be clear that communication is the very heart and soul of successful farm family transfers. If communication is **honest, direct, and clear**, the farm transfer can be a positive experience for all of the parties involved. If communication is unclear or if any of the parties involved mask their true

Daryl had heard a rumor that we didn't approve of the fans he bought and installed in the barn. Well, it wasn't true. We came home one night and he confronted us out in the yard about it. We had to tell him several times to come back and talk to us, get everything off his chest. We were afraid that with buying fans and the like that he'd over-extend himself. We'd gone without fans all those years. We told him we wanted him to be careful. It looks like a TMR is the next thing. It seems the fans are paying off, because he kept the production right up there during that hot spell. If the TMR lowers his costs, then that's a good investment.

Norma & Harlan Prestein

Last but not least. Keep lines of communication open. Talk, talk, talk. Remember "Please" and "Thank you." You're equal partners and working for the same goals. Don't take advantage of one another. A little smile or a squeeze in the barn aisle won't go unnoticed. And if family (parents) are helping, a thank you or a hug now and then means the world to them and makes you feel good.

Bev Brey

feelings, it's very likely there will be problems in the future. Regular meetings can be a useful tool for establishing and maintaining clear lines of communication. All parties need to recognize that changing circumstances require continual assessment and revision of goals. As in any successful business, communication needs to be regular, frequent, and on-going.

Lifestyle Choices and Philosophies: A Farmer's Viewpoint

As long as there have been changing generations, there have also been changes in lifestyle between those generations. One of the most difficult challenges in inter-generational farming operations is handling differences of opinion between two different generations— differences such as lifestyle, management, and investment decisions, to mention a few.

As a son or daughter becomes more involved in the day-to-day detailed decision making, they will begin to form opinions about how things should be done. Quite often those ideas will be different from what was considered “the way we do things around here.” The next generation may begin to challenge traditional ideas and methods of farming. One of the most frequent areas of disagreement concerns work. How many hours in a day? Why do we have to work weekends? Let's not cut hay now—the fair's on the next couple of days. Is work all we do around here? Be prepared. These discussions will come up.

Often, it may be a son's spouse who asks these questions of her husband (putting the son in the middle between Dad, who sees all the work that needs to be done, and the wife, who simply would like to spend more time with her husband). These issues must be discussed before they become full-blown conflicts. One of the best ways to avert this kind of conflict is through the process of goal-setting.

A family meeting called specifically for the purpose of goal-setting usually works the best. Try writing down your individual goals and then your business goals. Have everyone involved in the farming operation write down their goals and bring them to the family meeting. Reflecting on the goals before

meeting will be helpful. Some people find it difficult to speak publicly about their goals, and in this case, they can simply read them. This process will help everyone understand each other better.

This process is also very useful in intergenerational transfers and non-relative transfers for several reasons. First, the reflective time spent thinking about what your goals are will help you to clarify those goals and think about how to achieve them. Writing goals down provides you with a point of reference during in-depth family discussions. Last, it provides you with a written reminder of what your goals are for future reference.

The goal-setting process will help the other people in the discussions understand your reasoning in certain decisions. It will help you understand the perspective of others— especially important between entering and exiting farming parties, as the needs of the two parties to the agreement may be very different.

Farm Meetings

“Where are we going, Gamma?” my three-year-old grandson asked me as we headed out to get the cows. When we turned around to go back home, I asked him how we would get back home. He stopped for a moment, looked around in the pasture, and ran down to the cowpath and said, “cowroad,” as he called it, and we ended up back at the barn where we wanted to be. As I looked at the pasture, I saw several alternative cowpaths, depending on what area of the pasture you wanted to be in. However, they all came back to the main cowpath that took the cows to the barn.

My grandson's question as to where we were going is one that people should ask themselves more often. Think about each person's contribution to your farming operation. There may be several people involved in doing different things, each having different styles of how they accomplish their work, but does everyone have the same goals? Does everyone even know what the goals are?

Farm meetings are important:

- They provide a place where open communication can take place. Good, open communication is the key both in business and personal relationships.
- They can build the self-esteem of the people who work together, giving them value as part of a team.
- They provide a working model for everyone; people involved can use this model in their own families to build communication skills and broaden understanding.
- It is important to have regular meetings. That way people know that if they have an idea or a complaint there will be a time and place to discuss it. It helps people be more creative. You may not think there is any reason for a meeting, but you can't read other peoples' minds. Often some persons will have things they need to talk about when others feel there was no reason to meet on a particular day.
- It is extremely important to have someone take minutes of the meeting. It is something that is easy to overlook, but it is of utmost importance. Weekly documentation of discussions inventories, decisions, and contracts with hired help can be valuable documents, especially in dealing with the legal settlement of an estate. By keeping minutes, families are building a farm history helpful in making decisions for now and the future. Minutes are also useful to settle questions of disagreement as to what was said or decided.
- It can be important to share the minutes with others who aren't able to attend. This can help with building trust with spouses not as closely involved in the farm operation or others who are unavailable for a particular meeting.
- Farm meetings are valuable when it comes time to meet with the lender. It shows your administrative and leadership style. It will also give you more confidence when you present your financial and farm plan to the lender.

Calling the Farm Meeting

The following are some guidelines and ideas that you may want to consider as you prepare to start having farm meetings.

- Why is it important for your farming operation to have farm meetings? Name some benefits. Ask others who work with you for ideas.
- What would you have to do to get a farm business meeting to work at your farm?
- Who should attend? Who will be able to vote and make decisions?
- Who will chair the meeting? Will that leadership be shared?
- Where is the best place to meet? The kitchen table, or someplace else? Having records and other supplies available may be something to consider.
- When? How often should you meet? Meeting more regularly and for short, predetermined times is sometimes better.
- Setting an agenda is helpful. Find ways for others to put things on the agenda ahead of time too.
- Remember to have someone keep minutes of the meeting. A spiral notebook works well as it keeps everything orderly. Copies of the meetings sent to everyone may be appreciated.

Sample Agenda

It can be as easy as:

A. Attitude and agenda

B. Basics and barriers (naming them and then problem-solving them)

C. Communication and caring

Farm family transition conferences have revealed the following insights farm families have gained about family meetings. Here's what each group was concerned about:

Fathers

Agenda Items:

- Who will make the decisions?
- What are the job descriptions?
- What about vacation?
- How do we do problem solving?
- How do we keep people informed?

Barriers to Scheduling Meetings:

- Everyone's too busy.
- When and where to have the meeting.
- Why do a meeting now?
- We've never done one before.
- Can I let my son make the decisions?.
- How can I delegate responsibilities?
- I still want to be the boss.
- Fear that the meeting will be unproductive.
- Fear that there will be confrontation.

Compliments I would like to hear:

- Dad, you have done a good job!
- You have a lot of experience, Dad.
- You have a positive attitude and an open mind.
- Statements that show respect and consideration.

Mothers

Agenda Items:

- Finances.
- Family needs.
- Individual needs.
- Who's responsible for what?
- Short- and long-term goals.
- People's feelings.
- Vacations.
- Family health.
- Regular schedule of meetings.
- Transferring the farm to the younger generation.
- Selecting legal advice.
- New ideas.

Barriers to Scheduling Meetings:

- Making time for a meeting.
- Feelings and personalities (including children's and in-law's).
- Fear and resistance.
- Cultural (generational) differences.
- Having everyone feel equal.
- Not being able to give and take.
- Anger.

Compliments I would like to hear:

- Thank me for a good meal.
- Compliment me when I look nice.
- Say thank you.
- Listen to my management ideas.
- Give me an extra hug and kiss.
- Compliment my personal skills.
- Show respect.
- Say how much I'm needed.
- Acknowledge my accomplishments outside the farm.
- Accept me.

Adult Farm Children

Agenda Items:

- Where do I fit in—my identity as a partner?
- Discussing my own vs. other family members' goals.
- When do I get time off?
- Time to air what's bothering us—gripes.
- Time to dream out loud.
- Talk that separates the family from the farm.
- Discuss why we are having a problem.
- Inventory personal property.
- Where do all the kids fit into the family farm picture?
- Designate responsibilities—who does what.
- Discuss wage/pay issues.

Barriers to Scheduling Meetings:

- People are afraid to open up—there's a taboo on discussing feelings.
- Older generation is not practiced at open discussion/communication—people fear confrontation.
- Different kinds of personalities.
- Options aren't obvious.
- The notion that we've never done this before - why start now?
- Different values and attitudes.
- Fear that changes will cost too much.
- Situation is so overwhelming, it's hard to even get started.

Compliments I would like to hear:

- I am a good mother/father and wife/husband.
- My milking abilities are appreciated.
- I am a good leader.
- One son said that he got one compliment each day and how much that meant to him.
- "Thanks! You did a good job."

- How did things go for you today?
- Give me credit for innovations.
- For parents to say to me, "I was wrong, you were right."
- "That's something I didn't think of."
- "Take two days off - I'll do the work."
- "We're giving you a raise!"

Spouses of Adult Children

Agenda Items:

- What direction is the farm going?
- Who all wants to be involved?
- What are the feelings toward the farm and other family members?
- Where do I fit in?
- What are my rights?
- I want to learn—teach me.
- Can I influence decisions?
- Making time for my spouse.
- When will the transition occur?
- Where will we live?
- What will the financial arrangements be?

Barriers to Scheduling Meetings:

- Financial barriers.
- Who decides what direction the farm is going?
- A lack of trust.
- Non-family members.
- A lack of security for the in-laws.
- Lack of communication.
- Lots of people to consider.
- No time.
- Not knowing the father-in-law as a person.

Compliments I would like to hear:

- Make me feel welcome.
- Acknowledge my contributions.
- Treat me as a family member, not as an in-law.

- Ask for my ideas.
- Smile at me.
- Tell me that you appreciate my interest in the farm.
- Tell me I make an important contribution.
- I deserve a vacation.
- I did a good job.
- You give me the opportunity to have a sense of belonging.

Finally, look at farm meetings from your perspective as a tiller of the soil and follow these instructions:

Prepare seedbed properly. Plant seeds at the right time, nurture with tender love and care, fertilize with environmentally sound practices, watch carefully, check for temperature, moisture, disease, and treat disease when needed, recognize that you will reap what you sow, watch for signs of maturing, prepare for harvest, and bring everyone together to celebrate the harvest -

Successful Farm Meetings!

Goal Setting/Action Planning

Directions: Establish a clearly defined goal and target date, then outline the action steps necessary to reach this goal and identify a target date and person(s) responsible for each action step.

Goal (be specific): _____

Target Date (again, be specific) _____

Action Steps	Target Date	Person(s) Responsible
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1. _____		
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2. _____		
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3. _____		
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4. _____		
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5. _____		
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6. _____		
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7. _____		
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8. _____		
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Agreement: I/we recognize that our future depends on the goals and action steps outlined above. I/we agree to carry out this plan or modify it if it proves to be unrealistic.

_____	_____
Signature	Date

_____	_____
Signature	Date

Lifestyle Values and Choices - A Survey for Younger Farmers

Directions: Rate the importance for you of each item listed below by circling the number (1=not important; 2=important; 3=very important). Then discuss each item with your spouse and/or other family members. Use the survey to become clear about what is most important to you and your family in the farm transfer process.

		<i>Not Important</i>	<i>Important</i>	<i>Very Important</i>
1.	It's important for me to have money for vacations, for fun activities, and for home improvements.	1	2	3
2.	I am willing to make sacrifices and plow farm income back into the farm in the first few years of farming.	1	2	3
3.	I am willing to make sacrifices but I also want to honor my family's needs for spending money now.	1	2	3
4.	I want our children to grow up experiencing the responsibility and other benefits that a farm has to offer.	1	2	3
5.	I want to build a farm and estate that I can pass on to my children in future years.	1	2	3
6.	It's important to me that the farm and machinery we buy or use is safe for us and our children.	1	2	3
7.	I want to maximize <i>production</i> and will use the technologies which will allow me to meet this goal.	1	2	3
8.	I want to maximize <i>profits</i> and will do what I can to increase income, cut expenses, and meet this goal.	1	2	3
9.	I am willing to sacrifice production and/or profits to farm using sustainable methods.	1	2	3
10.	I believe you can maximize profits and still farm using sustainable methods.	1	2	3
11.	I hope our children will want to farm and will do everything I can to pass the farm on to them.	1	2	3
12.	I hope our children will be able to leave the farm and find satisfying off-farm employment as adults.	1	2	3
13.	I want to support my children in their career decision regardless of whether they decide to farm or not.	1	2	3
14.	I hope our farm will continue to be farmed after I/we retire in future years.	1	2	3
15.	It's O.K. with me if our farm goes out of production when I/we quit or retire.	1	2	3
16.	I view other farmers in our area as competitors and feel I need to be guarded in my interactions with them.	1	2	3
17.	I view other farmers in our area as resources and feel I should be reaching out to work with them when possible.	1	2	3
18.	My primary responsibility is to my farm and family; I don't have a responsibility to be active in community events.	1	2	3
19.	While my farm and family take priority, I also have a responsibility to be active in community affairs.	1	2	3
20.	Farmers need to be actively involved in community affairs if our rural communities are to remain alive and vital.	1	2	3

Developed by Roger T. Williams for Family Farm Transfers: A Guide for Exiting Farmers.

Name: _____

My Wants, Hopes, And Wishes For Our Farm Operation
An Exercise for Intergenerational Farm Transfers

Directions: If you are not clear about expressing your wants, hopes, and wishes for your farming operation, it's unlikely that they will materialize. Jot down your personal wants, hopes, and wishes in the following areas:

1. **Legal arrangement:** Would you like an outright transfer, a gradual transition, or some form of partnership/corporation?

2. **Financial arrangement:** What is your vision for how finances will be handled?

3. **Roles and responsibilities:** How would you view the transition of responsibilities?

4. **Personal relationships:** Are you hoping for a close personal relationship or more of a business relationship?

5. **Regular meetings:** Do you envision meeting on a regular basis? How often? Where?

6. **Problem solving:** How would you envision solving problems as they arise?

7. **Hopefulness:** How hopeful are you that your needs will be met through this transfer?

Lifestyle Values and Choices - A Survey for Retiring Farmers

Directions: Please rate the importance—for you—of each item listed below (1 = not important; 2 = important; 3 = very important). Then discuss each item with your spouse and/or other family members. Use the survey to become clear about what is most important to you and your family in the farm transfer process.

		<i>Not Important</i>	<i>Important</i>	<i>Very Important</i>
1.	I want the farm to remain in our family's possession.	1	2	3
2.	I want the farm to continue to be farmed after I/we retire.	1	2	3
3.	I want to keep physically involved after I retire from farming.	1	2	3
4.	I would like our children to play a part in the continuation of the farm.	1	2	3
5.	I would like the division of farm property among our children to be equal in dollar value.	1	2	3
6.	I would like the division of farm property among our children to be fair (not necessarily equal).	1	2	3
7.	It's important that my spouse and I agree on the plans for transfer of the farm.	1	2	3
8.	It's important that my spouse and I have enough money for retirement.	1	2	3
9.	I want to have the financial resources to do new things after farming.	1	2	3
10.	It's important that our children agree with our plans for the farm's future.	1	2	3
11.	I would like to be able to help our children establish themselves in careers outside farming.	1	2	3
12.	I want to be able to give financial help to our children who choose a nonfarm career.	1	2	3
13.	I want to be able to give financial help to our children who choose a farm career.	1	2	3
14.	I would like to maintain some financial control over the farm throughout my life.	1	2	3
15.	I would like to be involved in decision making for the farm throughout my life.	1	2	3
16.	I would like our children to play a part in the decision making for the farm's future.	1	2	3
17.	I would like our children to assist in my/our plans for retirement.	1	2	3
18.	I want to receive what our farm is worth when it is transferred.	1	2	3
19.	It's important to me that our children take over the management of the farm.	1	2	3
20.	It's important to me that our children choose farming as a career.	1	2	3
21.	It's important to me that our children have the opportunity to choose a career outside farming.	1	2	3
22.	I want our children to have the opportunity to continue the operation of the family farm.	1	2	3
23.	I would like everyone in the family to be satisfied with the way the farm/estate is handled.	1	2	3
24.	It's important to me that our children's requests regarding the farm transfer be honored.	1	2	3

Adapted from *Family Farm Transfer Planning* developed by Manitoba Agriculture and the Federal Business Development Bank in Manitoba, Canada

Chapter 3

My Farm

What Are Your Goals

Successfully passing down the farm is a complex business. It is important to follow objectives and goals when planning and implementing the transfer. It is also important to continue to review the objectives and goals throughout the transfer process to make sure they are being met.

Four Objectives/Goals to Remember When Doing a Farm Ownership Transfer

- That the senior partners selling assets to the family taking over a farm operation are taken care of for life. That they can live comfortably, have a good retirement plan and cash flow and not have to depend solely on social security. Also, to make sure that during the time of the transfer they don't feel anxious that the younger couple won't be able to pay them on an installment sale. If the senior partner is not assured of financial security, no transfer succession plan is secure.
- That the younger couple can live comfortably and can run a cost efficient, strong cash flow operation. The transfer must be realistic. The business must be big enough and good enough to cash flow successfully.
- That you will be good business partners and/or maintain a close family relationship and remain good friends during the entire time that you are involved in the financial agreement.
- That you will do the transfer with the least amount of tax liability for both parties.

An ideal goal with farm ownership transfers is to have the junior partner buy the personal property and try to have as much of the personal property paid off as possible by age 35 or 36, and then begin to purchase the real estate.

farm life

We have tried to be very fair. You have to be careful planning the arrangement, so you don't give them (the young couple) so much that you can't live decently yourselves, but on the other hand, burden them so much that they don't want to farm anymore. We made sure they were walking into an operation that was paying its way.

Delores Brey

We knew that if we sold the farm outright, we'd get hit real hard with taxes. Besides, Daryl couldn't buy the farm outright anyway. We were just like them when we started out—we didn't have anything either, so we wanted to help a young couple get started out in dairying.

Harlan Prestein

So in April [of 1994] we sold our cows on a five-year contract. They came with four heifers of their own, so by the time they started paying on the herd, they had 24 cows [four of their own heifers, plus one heifer a month for two years from Presteins.] As soon as the cows are paid off, then they'll buy the machinery. He pays for any machinery repairs. We pay the property taxes.

Harlan Prestein

My Farm Finds Me

In intra-family farm transfers, members often already know the physical and production characteristics of a farm but often do not know what the dreams, aspirations, and goals of each family member will be. It is very important in intra-family farm transfers that the family works together to answer farm management/ ownership transfer questions as individuals and then come together to share their answers as a group.

Below is a list of farm management and ownership questions to be answered by family farm members. These should be answered as individual families, then brought in and shared so that all members of the intra-family farm transfer know how each other feels. Meetings to discuss these questions may become emotional at times, but it is very important to talk about the answers to these questions openly prior to putting your name on the dotted line in any farm transfer. If these questions are well thought out, well discussed, and communicated to all members, you will be a step ahead of other farm families in working towards long term continuity and security in the farm transfer process.

Farm Management Questions to be answered by Family Farm Members

1. Can the family farm cash flow at its present size? If not, how can we make this operation cash flow? Is it viable to:
 - Expand the operation.
 - Expand and diversify the operation.
 - Stay the same size and become more efficient.
 - Have a partner(s) leave the operation.
 - Split the operation into satellite farms.
 - Keep the farm the same size and add alternative enterprises to the operation.
2. What is the best way to handle this farm family transfer legally? Is it best to do?
 - Sole-proprietorship.
 - Personal property partnership only.
 - Real estate property partnership.
 - Joint tenancy.
 - Corporation/Sub-Chapter S or Limited Liability Company.
3. Can all of the key players of the family farm communicate openly with one another? Areas that will need to be addressed are:
 - Job responsibilities; who will the lead person be in what area?
 - Vacations; time off.
 - Management decisions.
 - Records and sharing.
 - Authority to contract, borrow money, etc.
 - Who pays bills; who signs checks?
4. How do we work the grandchildren/future generations of this farm into the operation and how can we make it equitable to them until they are eighteen as far as chores, compensation for labor, showing cattle, involvement in activities, etc.?
5. What is the best way for Mom and Dad to transfer the farm? How can we make sure Mom and Dad are going to be financially sound for the rest of their lives and well taken care of? What is the best way to do an estate plan, will, etc.?
6. What roles do the spouses play? How do we treat the spouse who wants to work on the farm on a daily basis versus the spouse who would prefer to be a homemaker or get a full- or part-time job off the farm? How do we work at not building up resentment as far as equitable physical labor, mental stress, and financial commitments are concerned?
7. Where do the nonfarm children fit in? Where do nonfarm children fit into the estate plan, will, early inheritance, ownership of assets, etc.?

8. How do we ensure that the farm will stay secure if any of the following would happen?
- A divorce among any of the farm partners.
 - A farm partner decides to leave the farm six, ten, or twenty years after the business arrangement has been made.
 - Do we have/or need marital agreements?
 - What happens upon the death of one of the partners?
9. What about sweat equity? Should family members receive more compensation than other family members because of their longer commitment to the family farm as far as management and physical labor, along with financial commitments?
10. What are your goals for the next five years; the next twenty years; your lifetime goals and your visionary plan? Will your individual needs be met in a partnership or corporation business arrangement?
11. How many acres and cows do you think one person can handle?
12. How much time off do you want? How much time off is fair?
13. Who will live on the home farm? How should meals be handled for employees or family members working on the main farm but living elsewhere? Where should all parties and employees be housed?

farm life

You've got to know your party, know their background, their sincerity. We knew Daryl and his family [he is from the area], and knew how he worked up at the neighbor's. We knew he meant it when Daryl said he didn't want to work in town.

Harlan Prestein

It hasn't been a problem that he's not a family member. In fact, maybe it's been an advantage. In some families people don't get along at all. We knew our boys, they didn't want to be told what to do. If people won't listen, then it won't work. Life's too short to spend your time fighting.

Norma Prestein

I Find My Own Farm

Farm transfers between unrelated parties are treated in a very different light than transfers within a farm family. Unrelated parties must work very hard at building trust and respecting each other's farm management styles and lifestyles. In addition, unrelated parties must learn to adapt to each other's visionary plans for the farm and work together to set goals.

There are many questions to ask when looking at purchasing/renting farm real estate. Those questions are as follows:

Questions To Ask When Looking At Purchasing/Renting Farm Real Estate

- Municipality or Town farm is located in; ag zoning policies.
- Is farm enrolled in Farmland Preservation?
- Amount of annual real estate taxes paid.
- Are real estate taxes paid/current on farm?
- FSA—Is the farm enrolled in any government programs? Is any part of the farm eligible for the Conservation Reserve Program (CRP)?
- NRCS—Does farm have a soil and water conservation plan? Does it meet the requirements of the 1985 Food and Security Act?
- Soil tests—pH level of soil.
- Water nitrate level—ppm?
- Grade A or Grade B milk?
- Where is the well located? Up to code?
- House - flush toilet: septic system or mound system? Roof in good shape, insulation, overall shape of home on the farm.
- Price of the farm.
- Price to rent real estate. If you rent, is there an option to buy?

- Is there a second house on the farm? If so, will the present owner live in it permanently? If so, is the house surveyed off from the property you would purchase?
- Are there any mortgages or judgments held against real estate you are purchasing?
- Environmental assessment - farm dump? surface water contamination? - underground storage tanks?

Questions To Ask When Buying Personal Property

Personal Property: Livestock, machinery, and feed (current assets).

Cows:

- Pounds of milk sold (actual) for the most current year divided by all cows in herd (look at daily milk slips).
- DHIA, RHA, protein test, and fat test.
- Quality awards/premiums.
- Visit with vet on herd health—past herd history. (You'll need current owner's permission)
- Has milking equipment been kept in good shape so there is no permanent damage to udders?
- Registered or grade?
- Hoof trimming program?
- A.I. - 100% bull requirements.
- Price.

Machinery:

- Type of machinery maintenance program farmer has been on.
- Price.

Feed:

- Harvesting method.
- Price/ton or bushel or acre.

Are there any liens against any of the personal property?

Once you've put together the transfer plan for your farm, review your goals once more to see if the plan you've developed best meets those goals. Then work with your lender, attorney,

accountant, realtor, or other professionals to execute the plan.

Setting goals, revising goals, and adjusting to change are vital keys to any successful farm transfer.

Farm Link

Retiring farmers who want to exit farming don't always have a family member who is able or willing to take over the family farm. Not having that built-in takeover often means farmers delay decisions about retirement and estate planning. Likewise, some young people who would like to farm don't have the family connection to get into farming. Wisconsin, like many other farming states, has developed a process for linking together retiring and beginning farmers.

Called **Farm Link**, the service is housed at the Wisconsin Department of Agriculture, Trade and Consumer Protection, Farm Center (800) 942-2474. Both retiring and beginning farmers complete applicant forms. In addition to requesting information on the physical plant, farm location, and historic enterprises, the questionnaire asks about particular interests a farmer may have and whether or not the buyer has financing or the seller can provide financing for the transfer.

Thereafter, a search is made of other applications to find possible matches or links. Information about the applicants is then forwarded to the matched parties. After that the parties meet and develop their own transfer plans. One match which is working well involves a beginning farmer with no assets who began as an employee for a two-year period. At the end of the two years, the parties were comfortable enough with each other's philosophy, work style, and contributions to start the transfer. The first step is underway, with the beginning farmer now purchasing the dairy herd.

Copies of current applicant forms are attached at the end of this guide. Questions on the forms can be a reminder to both entry and exit farmers on issues that need to be considered in any farm transfer.

farm life

Lots of arrangements don't work because people aren't flexible. But you have to make it fair for yourself too. Our contracts are set up so that if interest rates go up, the rate on our contract will go up too. [Adjusted every two years.]

People sometimes sell their whole farms. If the deal doesn't work out, they end up getting them back, with the buildings neglected and property taxes not paid up.

Harlan and Norma Prestein

Chapter 4

Farm Business Arrangements

Employment Relationships

Employees can be “at will” or contractual employees. An “at will” employee can be terminated at any time, without notice, and the employer does not need to provide a reason or justify the action to the employee. The employee is also free to resign at any time without giving advance notice to the employer. If an “at will” employee is terminated or quits, any wages due to the employee should be paid in full, no later than they would have been paid if the employee remained employed.

An “at will” employment relationship does not require a written agreement between the parties. If an employer wants to maintain an “at will” employment relationship and provides the employee with a written handbook or other written information about compensation, fringe benefits, work rules, etc, it is important that the written information include a disclaimer that the written document does not constitute an express or implied employment contract between the parties. In addition, the handbook should not require two weeks notice when the employee quits.

A contractual employee is one who has been hired under a written contract or under circumstances creating an implied contract for employment. Generally, a written contract for employment will include compensation, fringe benefits, and other terms of employment. The contract will usually specify the conditions under which an employee can be terminated and will include notice or other requirements when the employee resigns his/her position. The contract provides clarification of the employee/employer relationship for both parties.

An employer can create an implied contractual relationship. An employee handbook that covers terms of employment, procedures and expectations for employees, conditions for termination, etc., can create a contractual relationship between the employer and the employee. To prevent the

employee contract from being considered an implied contract, the employer should include a disclaimer within the handbook clearly stating that the handbook does not constitute an express or implied employment contract.

Employee Compensation

There are a variety of methods of compensation used for farm labor. They include cash, fringe benefits, incentive payments, bonus payments, and commodities. A compensation package can involve a single type of payment or may combine several types of compensation. Creative use of the various types of compensation can allow the employer to offer the employee a higher overall level of compensation or may be used to provide incentives to the employee for above average performance. A brief description of each type follows.

Agricultural employees will generally receive at least a portion of their compensation in cash wages. Employers may set the compensation level for their employees as long as the amount paid complies with minimum wage laws for agricultural employees. Cash compensation is generally stated in terms of an hourly, weekly or monthly amount. Wages can be paid weekly, biweekly, or monthly. The level of compensation provided is generally dependent on prior job experience, the skill level of the employee, and the duties of the job. Higher skill requirements, managerial and supervisory duties will command higher compensation than general farm labor. Other types of compensation the employer is providing to the employee may also affect cash wages. In determining whether or not the minimum wage laws are being complied with, all compensation paid to the employee will be considered.

For many employees fringe benefits are as important as cash compensation. Common types of fringe benefits for agricultural employees include meals, food, housing, utilities, health insurance, disability insurance, life insurance, payment for vacation and sick leave, and contributions to retirement or pension accounts. Fringe benefits can be costly for the agricultural employer; however, they may be a significant

factor in employee retention. In many cases, since fringe benefits are generally non-taxable, both the employee and the employer can benefit from the inclusion of fringe benefits in a compensation package. Benefits such as health insurance, disability insurance, life insurance, and sick leave can reduce stress because they provide protection for the employee and his or her family. The use of non-taxable fringe benefits can reduce the employee's overall tax burden and may also allow the employee to qualify for an earned income credit. It is important that at the time of hiring, both the employer and employee have a clear understanding of what fringe benefits are being provided and the cost of those benefits, if any, to the employee. This may be included in a written employment contract. If the employee is an "at will" employee, the employer should make sure that the employee is clearly informed about the benefits that are being provided. If the employer does not want to establish a contractual relationship, a disclaimer should be included in any written document given to the employee clearly establishing that the written information does not constitute an express or implied contract.

An employer can use incentives to encourage efficiency and high level performance. If an employer uses an incentive plan, it is important to clearly identify the performance standards to be used when reviewing the employee's performance. The standards should be reasonable and achievable so that the employee has the potential for meeting them. An employee who has a stake in profitability will generally be more likely to look for ways to improve his/her efficiency and quality of work. If, however, the employee finds that the standards are unrealistic and unreachable he/she may become resentful and unhappy with his/her job. The goal of an incentive program is to make both the employee and the employer better off for the incentive plan to work. The incentive plan includes goals over which the employee has control. It should be as simple as possible, so it can be easily understood by both the employer and employee. In establishing incentives, the employer should examine the current situation and base any incentives on improving or maintaining that level of performance. For example, an incentive plan

for a herdsman might be based on increasing or maintaining milk production at a particular level. The goal for the herdsman would be different for a herd with 12,000 lbs./cow/year average production vs. one with a 30,000 lbs./cow/year average production. The employer with the lower average will want to see an increase in the production level before the incentive comes into play, while the second employer may only want the employee to maintain production levels and milk quality.

Bonus payments are not the same as incentives. They should not be based on improving or maintaining performance. Bonus payments are sometimes dependent on the net income of the employer. When the employer has had a good year, bonuses may be greater than if the year has been more difficult. Bonuses are often paid at the end of the year and are commonly referred to as "Christmas bonuses." Bonuses may also be given for length of service with the employer, as payment for unused sick leave or vacation at the end of the year. If there are conditions for bonus payments, they should be made clear at the time the employee is hired. If the employee anticipates receiving a bonus and does not receive one or receives substantially less than anticipated, the employee may become resentful if he/she has an expectation that the bonus is part of his/her package of compensation.

Some or all of a compensation package can be paid in the form of commodities, such as grain or livestock, rather than cash. Unless the parties are very careful, the transfer of commodities can be treated as equivalent to cash wages. The factors that establish the transfer as non-cash compensation include the following: 1) There must be sufficient documentation to support the transfer from the employer to the employee, 2) The employee must take responsibility for all marketing decisions regarding the commodity, 3) The risk of gain or loss must shift from the employer to the employee, 4) The employee must bear all costs of ownership including storage fees even if they remain on the employer's property, 5) The commodity must be readily identifiable, and 6) The commodity should remain in the employee's ownership for some amount of

time after the transfer. Be aware that where the facts indicate the practical impact of the transfer was the same as paying the employee in cash, and the payment of commodities as wages seems to be for the purpose of avoiding social security taxes, the entire payment may be treated as cash wages.

Considerations when Renting Property

Renting property can be a good alternative to purchasing, especially for a beginning farmer who has limited financial resources. Farm real estate, buildings, machinery or livestock can all be leased. The farmer who is renting the property, the tenant or lessee, pays the owner, the landlord or lessor, an agreed-to amount of money as rent for the use of the property. Property can be rented under either a written or oral lease. A written lease is generally preferred because it documents the full agreement between the parties. It can not only help the parties avoid disagreements regarding the terms of the lease but can also help resolve any disputes the parties may have regarding the lease. Finally, the lease can provide protection for both parties in the event of a sale of the property or the death of one party.

Real Estate Leases

Farm real estate is the most common type of property leased by a farm business. Keep in mind that every lease situation is different and that every lease term can be negotiated between the parties. If the operator or the owner of the real estate participates in USDA farm programs, a written lease may be required to verify eligibility for program benefits.

Agricultural leases generally begin on March 1st and end on the last day of February the following year, although the parties can agree to any starting and ending date. A lease may be oral or written. An oral lease or periodic tenancy covers a one-year period. Often oral leases continue year after year as long as the landlord and tenant continue the arrangement. To terminate an oral lease, one of the parties has to give a 90-day written notice prior to the end of current year or the lease will continue for another year. A

written lease can specify an alternative method of notice for termination.

There are three types of farm real estate leases:

- cash
- crop share
- livestock share

Cash Leases for Real Estate

In the cash lease, the tenant pays the landlord cash for the use of land and/or buildings. Typically the landlord pays all of the fixed costs (property taxes, interest, insurance on buildings, repairs on buildings and fences); however, with a written lease, the parties can agree to have the tenant assume responsibility for all or part of the fixed costs in exchange for a reduced rent. If the tenant pays for expenses, these amounts are still considered as a rental expense to the tenant and as income to the landlord. Generally the tenant pays all operating expenses. The tenant receives all of the income from the sale of farm products. Although the landlord may have a lien for the payment of rent, he/she does not own an interest in crops or other products produced by the tenant.

A cash lease provides the tenant with a great deal of control over the real estate as long as the tenant's actions are in compliance with the terms of the lease. The tenant bears the risk of gain or loss from the farm operation. Even if the crop fails or the business loses money, the tenant is still obligated to pay the landlord the agreed-to rent for the property.

Crop Share for Real Estate

In a crop share lease, the landlord and tenant share in both the risk of loss and the potential for gain on crops produced on the farm. One of the main characteristics of a crop share lease is that decisions are made jointly with input from both the tenant and the landlord. Costs such as property taxes, insurance, costs related to equipment used in the operation, seed, fertilizer, and fuel, etc. are assigned between the parties per the lease agreement. A typical crop share lease may provide that the landlord is responsible for costs related to the real estate (i.e. property taxes and insurance), the tenant is

responsible for all costs related to purchasing and maintaining insurance, and the parties split planting and harvesting expenses 50/50. Income can be divided in any percentage agreed to by the parties with a 50/50 split being the most common.

Livestock Share for Real Estate

A livestock share lease involves both crop and livestock enterprises. In a typical lease, the landlord owns the real estate and half of the livestock. The tenant owns all of the machinery and the remaining half of the livestock. The tenant provides all the labor for the entire farm operation. All farm income is split equally between the landlord and tenant. The landlord generally pays fixed costs for the real estate. The tenant typically is responsible for expenses related to purchasing machinery and livestock and for expenses related to farm labor. Other livestock and crop expenses are split equally.

With a livestock share lease it is best to have a written list so that the rights and duties of both the landlord and tenant can be set out in the lease. In addition to division of income, the parties should determine whether there will be any restrictions on crops, conservation practices, requirements to remain in compliance with USDA programs, zoning ordinances, upkeep of buildings, and any rights reserved to the landlord.

Careful crafting of the lease agreement can avoid misunderstanding and conflict during the lease term. Both the landlord and tenant need to know exactly what expenses they are obligated to pay and which party receives each of the various income items. For example, the landlord may pay half of custom-hired cropping expenses such as baling or chopping if the tenant does not own that particular type of equipment. Either party may own barn cleaners or silo unloaders and the expenses associated with them must be stated in the lease. Expenses can be shared in a manner different from the typical lease if both the landlord and tenant feel alternative terms make sense and are fair to both parties.

A livestock share lease involves the greatest shared management responsibilities of any type of lease. More risks in the livestock

share lease are assigned to the landlord; however, the return to the tenant is less because livestock income is also shared.

Machinery Leases

One way to acquire the use of machinery is through a lease arrangement. This is normally done through a farm machinery dealer. Not all dealers provide machinery leases. Leases with a dealer will generally be written leases and will include a variety of terms including the maximum number of hours the machine is to be used, any restrictions on the use of the machinery, etc. Machinery leases are generally for a cropping season or year. Occasionally, dealers will provide a longer lease but leases for longer than two years are rare. Machinery leases are generally used for expensive items such as tractors or combines.

A fixed lease payment is generally based on the use of equipment for a maximum number of hours. This may include a purchase option with all or a portion of lease payments being subtracted from the list price. The lessor normally provides for repairs in case of a breakdown; however, the lessee may be required to provide the labor to make minor repairs.

Before leasing machinery, a farmer should compare leasing costs to annual fixed ownership costs to identify the cheapest alternative. In some cases a lease may be cheaper than the fixed costs for purchasing new equipment.

Finance Leases

Finance leases are usually multiple-year leases. An individual selects a tractor, combine, or some other piece of machinery. The owner of the machinery receives payments from the farm producer for the use of the machinery. The owner retains ownership of the asset and takes the depreciation. The lease payment is fully tax deductible to the farm producer. At the conclusion of the lease period, the farm producer has an option to purchase the piece of machinery from the lender by making a payment agreed to at the time the lease is entered into. This payment is typically rather low. This option of financing can be cheaper than borrowing money for purchase of

equipment. The higher the prevailing interest rates, the more attractive this type of financing becomes.

Farm Building Leases

Farm building leases provide an alternative to purchasing or constructing a building. Alternatives include leasing from a farm construction company or leasing unused farm buildings from a neighbor.

Leases with construction companies are usually multiple year leases. Generally, a purchase option is included at the end of the lease period with a final payment agreed to by the parties at the start of the lease. This type of arrangement is generally used where the lessee is reluctant or unable to purchase the building. The lessor provides the lease option hoping the lessee will purchase the building at the end of the lease since it can be very expensive for the lessor to tear down the structure at the end of the lease period if the purchase option is not elected.

Leasing unused buildings from neighbors is typically much cheaper than constructing new buildings. Initial costs to update unused farm buildings can be very expensive and should be considered carefully before making the decision to enter into a lease. The tenant should obtain estimates before entering into a lease arrangement. If the lessee is expected to pay for upkeep or improvements, those anticipated expenses should enter into any calculations to determine whether or not the lease is a good choice for the potential tenant. To avoid conflicts about what expenses the landlord and tenant have agreed to, it is important to have the terms of any agreements stated in a written lease that is signed by both parties.

Livestock Leases

Options for leasing dairy cows or other breeding livestock from a leasing company or from a retiring farmer can be used to increase the size of the herd available to produce income. Lease payments are based on the number of cows leased. It is important to make sure that the agreement includes language related to the quality of the cows being provided under the lease, especially where the agreement gives the lessor the

right to exchange cows at any time during the lease period.

The lessor generally bears the cost of losses due to the death of leased cattle; however, after a certain point the lessee may be expected to pay for additional losses. Offspring born during the lease period typically belong to the lessor; however, if the stock is of a high quality the lessee may want to pay a higher lease payment and retain young stock. Feed and operating costs are usually the responsibility of the lessee. When calculating whether it is a better option to lease or purchase livestock, fixed costs of ownership should be factored into the formula to determine which is the cheaper alternative. As a general rule, a farm producer would be better off financially owning the livestock and leasing other assets. The return for the livestock investment is normally greater than for machinery or real estate.

Leasing the cattle from a retiring farmer may be more attractive than leasing from a leasing company for two reasons. First, the lease allows the retiring farmer to spread out capital gains differently than would happen with a herd dispersal sale. Second, the retiring farmer who has spent years building up a quality herd may be able to see his efforts continued by a younger farmer and not have to experience the emotional issues generated by a dispersal auction.

In some cases, a retiring farmer may be willing to lease livestock to a younger farmer as part of a package that includes land and machinery. A typical rental agreement may provide that the younger farmer will own young stock allowing for a gradual increase in the ownership of livestock over the period of the lease. The retiring farmer would receive income from cull cows allowing income to be spread out over the lease. By keeping income at a more level rate, the retiring farmer may be able to minimize tax consequences when compared with a complete dispersal of cattle and machinery.

Since the younger farmer is leasing the livestock and machinery this arrangement may generate some conflict between the younger farmer and the retiring farmer. This is especially so when the retiring farmer may

be having difficulty letting go of the farm operation. To increase the chance for success in this type of arrangement it is advisable to have a plan in place to address conflict between the parties.

Forms of Business Ownership

There are a number of forms of business ownership, including variations and hybrids of each type of ownership, available to farm business operations. The most common form of ownership in farming is still the sole proprietorship. Other forms of ownership, however, may be more attractive depending on the goals of the business at any given point in time. For example, a goal of helping adult children establish a separate farm without having to carry a heavy debt load is very different than a goal to retire from farming in a way that will minimize tax consequences. Although each of these farm owners may choose a business operation that looks similar in some ways, the goals of each should drive decisions regarding the type of operation used in each situation.

It is important that farmers take the time to develop a business plan, set goals and then determine the best type of ownership to carry forth that plan. Once the goals of the operation have been identified it is advisable to seek the advice of tax, accounting and legal specialists so that the enterprise is set up to provide the best opportunities for success. Please keep in mind that you should seek specialists who have knowledge and experience working with farm businesses because they are familiar with the special issues related to operating a farm business.

Although some forms of ownership, such as a sole proprietorship, are very easy to establish, there may be significant personal, financial, legal or other reasons to enter into a more formal type of operation. Although it is easy for a new farm business to set up a particular form of ownership, it is equally important for existing farm business operations to consider the pros and cons of changing the current ownership structure.

Problem Solving

With any form of farm business ownership, including the sole proprietorship if more than one individual is involved, the individuals

involved will need to address problem solving and decision making within the business operation. Especially since a variety of personalities are involved in the business, a clear process should be established before problems arise.

Consideration should be given to the following: a) Which decisions will be made unilaterally by one party or another, which require agreement of one or more parties, which require unanimous agreement? b) Will anyone in the business have sole authority over certain issues and if so what issues are included? c) How are "voting rights" established? Are they based on ownership, and if so, does the party who only provides management and labor have any say in decisions? d) Will meetings be held, and if so, how often and who will schedule and chair the meetings? e) What happens if the parties cannot reach agreement? Is there a dispute resolution clause included in the business documents?

Consider the following examples: The parties, parents and their adult son, agree to work together as partners. When the operation first begins, the son has a small herd of dairy heifers that brings in no income. The parents own all other equipment and cattle in the operation. The son agrees to apply for operating capital along with his parents, and will provide approximately 75% of the labor in the operation. The parties agree that the son will receive 40% of the net income from the operation and the parents 60%. Several years down the road, the son's heifers have all been added into the dairy herd. In addition he has purchased additional heifers and cows from a herd with historically high production levels. He now owns about 50% of the cows. He is still providing 75% of the labor for the operation. The son feels he should be getting more of the net income, but the parents feel he shouldn't because they still own most of the assets used in the operation. They are happy that he is making progress in increasing his share of the dairy herd; however, they know that he probably wouldn't have been able to do this if they hadn't been providing him with free room and board. They are also still jointly responsible for borrowing operating capital. As long as the parties are willing to sit down and discuss

whether the current percentages are still appropriate and reach a mutually acceptable agreement, this operation will continue to work. If no agreement can be reached, how will the differences be resolved? Without any plan to resolve disputes, and no plan for terminating the operation in the event that both parties want out, the parties will be at a standstill.

Take the same example as above and assume that the son and his parents were able to resolve the first problem by increasing the son's share of net income to 45%. Two years later, their son marries and within a year or so begins a family of his own. When he married, he and his wife rented a small house near the farm. Given the added expense resulting from his marriage and the birth of his child, the son needs additional income. He again approaches his parents to ask for more money. He now owns most of the dairy herd and several of the larger and more expensive pieces of machinery. He feels that he should be receiving at least 60% of the net income and his parents 40% or less. What if no agreement can be reached at this point?

Regardless of the type of business organization put into place, it is very important to consider problem resolution before any problems occur. It is important to put in place a mechanism for reevaluating contributions to the business as they change over time, for resolving disputes, for terminating the operation if it no longer works for the parties, and for dissolving the operation in the event of the sale of the farm business or the death of one of the parties.

Sole Proprietorship

The sole proprietorship is the most common type of ownership for farm businesses because of the simplicity and flexibility of the arrangement. A sole proprietorship can be established, modified, bought, sold, or terminated very quickly and easily. Often because of the mingling of business and household finances and operating with a resource base that is primarily the owner's net worth, there is little if any distinction between the owner's business and personal affairs. Generally a sole proprietorship is held by one person; however, a husband and wife or family can operate as a sole

proprietorship. Nearly all the legal rights and responsibilities of a sole proprietorship are considered to be one and the same as those of the individual, couple or family.

In a sole proprietorship all assets are titled and controlled by, income payable to, and debts the responsibility of, the sole proprietor. All profits accrue to, and all losses are borne by, the sole proprietorship. Assets may be owned outright or rented.

The sole proprietor has unlimited liability for debts and they can be satisfied by the personal assets of the owner. Lenders will often require signatures on debt agreements by both the proprietor and spouse whether the spouse is involved in the operation or not.

Limited Liability Company

This form of business entity is a recent development in Wisconsin. It has become popular with new farm businesses because it offers the simplicity of a partnership for income tax purposes, together with the limited liability afforded to corporations. One or more members can form an LLC. Profits and losses, the right to receive distributions of assets, and to participate in management of the LLC are determined by the member's interest in the LLC. One of the more attractive features of the LLC is that the owners are not personally responsible for the debts of the LLC; however, owners may be liable for unlawful distributions or if they fail to pay in contributions to the company according to the LLC's operating agreement.

Partnerships

Partnerships continue to provide a useful and functional business mechanism for running a farming operation. One of the most key factors in establishing a partnership is finding a workable process for dealing with decision-making. Partnerships involve parties who generally have a variety of personality characteristics, different skills and abilities, and different strengths and weaknesses. This is one of the best and the worst qualities of a partnership. The variety of skills and strengths is what makes the partnership more successful than the partners would be if they operated individually; however, the different ways of approaching issues, different levels of comfort

with risk, different temperaments, etc. can cause problems with the decision-making process.

Probably the biggest obstacle with the partnership as a form of business operation is the lack of any type of formal written document regarding the partnership. Often partnerships simply evolve through the operation of the farm business over time. It is often not until one of the partners becomes dissatisfied with the way the partnership operates that problems arise. Factors that can increase the likelihood of problems arising in a partnership include: marriage of one of the partners, the entrance of new partners, a significant increase in expenses or drop in income, and the need to make decisions regarding large investments of new capital into the business to keep it viable.

Frequently partners fall into key roles in the operation based on their skills and abilities. In the operation of the partnership those roles become comfortable and as long as each partner is comfortable with his or her role, the partnership will operate relatively smoothly. As circumstances change, those roles may also need to change. The young adult going into partnership with his/her parents may initially be comfortable providing labor; however, as he/she develops more knowledge and becomes more skilled in management he/she may want to take a more active role in making day to day decisions in the operation. If one child becomes a partner and some time later another child wants to join the partnership, the older child may feel that he/she has earned the right to be the boss where the younger partner is concerned. What happens when the younger sibling doesn't want to accept that role? Perhaps the older sibling did not go on to further his/her education while the younger child has a degree in business. Can the older sibling define the younger sibling's role in the partnership, or prevent the younger one from becoming part of the partnership?

These are all changes that a well-written partnership agreement can deal with. If there is no written agreement in place, the result may well be anger and resentment on the part of one or more of the parties. When emotions enter into the picture, the

partnership becomes more and more unstable until the emotions are dealt with. Regardless of whether or not day to day operations continue, in many cases the underlying anger and resentment will eventually doom the partnership.

Unfortunately, most farm business partnerships are between related individuals, whether husband and wife, parent and children, or siblings. When the partnership falls apart it has a ripple effect which can create havoc on the personal relations between the individuals in the partnership, and in many cases will involve other family members as well.

Even though the business may have operated without a written agreement for some time, it is still possible for the parties to sit down and identify individual goals to see if a compatible partnership can be developed. The partnership agreement should deal with how decisions are made regarding compensation of both full-time and part-time partners, their spouses, and other employees of the partnership. The agreement should deal with decision-making processes for both the operational and financial aspects of the partnership. The agreement should set forth a mechanism for keeping partners informed about what is going on in the partnership, how that information is provided, and how often. The agreement should specify how often meetings are to be held, what types of issues are dealt with in regular meetings, and what types require a special meeting of the partners. The agreement should specify what type of financial information is provided to the partners (i.e., financial statements, cost proposals for capital expenditures, quarterly comparisons of expenses, and income projections with actuals.). Although these may seem like common sense issues for partnerships, ignoring them will undoubtedly create problems that can ultimately destroy the partnership.

Independent Operating Agreements

Although operating agreements can be used in conjunction with other forms of business ownership, such as an LLC, the operating agreement can also be the form of business operation between two or more independent owners. An operating agreement, standing

alone, is not designed to establish a partnership or other type of farm business arrangement. It is useful for putting into writing the business arrangement between parties, but it does not impact the reporting of income and expenses. Each party reports income and expenses and files the return appropriate for his/her situation.

When the operating agreement is between sole proprietors, there is normally little or no joint ownership of assets. In an operating agreement between different generations of a family, the younger generation may provide labor, some management, and little or no capital assets at the commencement of the agreement. With an operating agreement the parties can easily separate the assets and terminate their operating agreement if the agreement is not working according to expectations.

Unlike a partnership, each party pays the fixed costs such as insurance, taxes, and interest on his/her own assets. Operating expenses are divided based on the allocation of resources provided in the operating agreement. The “Multi-Person Farm Operating Agreement Worksheet” can be used to estimate the contributions of each party involved in the operating agreement. This worksheet, form A2664, is available from any County Extension office.

Each party receives any income generated by the agreement according to the percentage of his/her operating expenses and contribution to the operating agreement. Income received from individually owned assets is paid entirely to the owner of the asset.

Enterprise Operating Agreements

An operating agreement can involve an entire farm operation or only selected enterprises. An agreement that covers selected enterprises is often referred to as an “Enterprise Operating Agreement”. An enterprise operating agreement is often used in operations which involve multiple generations within the family, where the younger generation family member owns machinery or livestock, or provides operating capital for one or more parts of a farm operation. The younger generation farmer also contributes part of the management and labor for the enterprise. The enterprise operating

agreement provides the younger farmer with a portion of the income from the enterprise that takes into consideration his/her capital contributions to the enterprise. This type of agreement provides an avenue for the younger generation to begin to establish capital ownership within the farm operation.

A common situation could involve a child involved in a dairy operation. The younger farmer may own a small herd of beef cattle. The enterprise agreement would recognize that ownership, and provide that the child would pay the expenses related to that operation and would receive the income from that part of the operation. The enterprise agreement would not provide for income from dairy, crop or other operations on the farm, but would provide labor towards these other enterprises.

Separate Farms but Working Together

Two separate farm operators who work closely together may decide to share machinery between both farms. Each farm operator is a sole proprietor with a separate income and separate expenses. The operators trade work with each other without exchanging money for labor. Machinery in this situation may be owned individually or jointly but other than machinery, there is no joint ownership of other assets.

This type of arrangement has worked well with parents who want to help a grown daughter or son get started in farming, or with siblings who operate neighboring farms. By sharing high cost equipment, the two operations can maximize the use of capital assets.

Where the equipment is owned by one party or ownership is not of equal value, the party owning less may provide additional labor. For example, if machinery is owned entirely by the parents, the adult child can provide additional labor for the use of machinery. This allows the adult child to enter into farming with a lower debt than if he/she had to purchase or lease all the machinery needed for the operation. Over time, the younger generation should be able to acquire additional machinery and eventually, if desired, be completely on their own. In other situations, it may be in the best interest of

the parties to continue to share expenses for machinery that will keep the capital investment costs lower for both parties.

Custom Farming

Custom farming, or contract-farming, is an opportunity to either provide some service for compensation or to acquire a service needed because of a shortage of labor, management expertise and/or capital to own specialized equipment. Under this arrangement one party provides a service to the other for a fee that has been agreed to by the parties.

An example of a contracting farming arrangement is raising heifer calves for an area dairy operator. The contracting party provides labor, management expertise, feed, supplies, building space, and the necessary equipment to raise replacement dairy heifers for a fee. Generally, the contracting party has excess labor and/or building space and can generate income from these unused or under-utilized resources. The contractor does not own the dairy animals. At maturity these animals are returned to the herd of the party paying for this service. Custom raising of feeder cattle or pigs is very similar to the raising of heifer calves. Another possible custom farming arrangement is for crop machinery operations. Sometimes the custom operator provides all the machine operations for the crops or provides selected machine operations. The most frequent selected machine operations are harvesting or spraying. For these machine operations, the custom operator receives a set fee for the service and does not receive a part of the crop produced.

Alternative Business Models/Land Trusts

Land trusts can provide important financial alternatives to both retiring and beginning farmers. A variety of tools can be used, including purchase of conservation easements, tax reduction planning for both income and property taxes, and shared equity mortgages. These tools can often be used along with conventional financing options.

By working with a land trust to sell their farm, retiring farmers may be able to realize a significant reduction in capital gains taxes, or to receive tax deductions that can offset

taxable income in current or future years. This may allow them to sell their farm at a more affordable price and make it easier to find the right buyer.

Some farmers in Wisconsin and other states find that land trusts can be helpful in planning alternative ownership models for farm transfers. Land trusts are private, nonprofit organizations that work to conserve farmland, open spaces, and natural areas. An elected board of directors usually governs them. Land trusts can have a national focus (i.e. American Farmland Trust) or a state and local focus (i.e. Wisconsin Farmland Conservancy). As IRS-recognized nonprofit organizations, land trusts may be able to offer landowners a number of options that can protect farmland and provide important tax and financing advantages.

Easements

In some cases, farmers can work with a land trust to establish conservation easements that will secure farmland for permanent agricultural use. The conservation easement is a legal agreement between a landowner and a land trust that protects the agricultural or natural character of a farm. An easement may either be purchased by the land trust or donated by the farmer.

When we own land, we also own many associated rights, such as the rights to harvest timber, mine minerals, and so on. When a farmer sells or donates a conservation easement he/she is agreeing to limit the use of some of these rights permanently. For instance, a farmer may agree to keep the farm in agriculture in exchange for a cash payment from a land trust or local government. The value of the easement is negotiated between the farmer and the land trust by appraising the land's value for either development or farming uses. In some cases, an easement might apply to only a portion of the farm, leaving the option of development open for the remaining part. Future owners are also bound by the easement, and the land trust is responsible for monitoring its terms. Easements do not have to require any public access.

Farmers who want to protect their land, and receive tax savings may also choose to donate a conservation easement to a land trust. To

meet federal tax code requirements the easement must, in essence, provide public benefit by protecting important conservation resources permanently. The farmer may consider the value of the donation as a tax deduction on income or capital gains taxes. If a farm near an urban area is valued at \$400,000 for development purposes, and a conservation easement is placed on it that drops its value to \$200,000 for agricultural use, the value of the donation is \$200,000. This deduction can be used to offset income from the sale of other assets, investments, or employment.

Even farmers in areas without development pressure may benefit from the donation of easements, especially if they face significant capital gains taxes and wish to establish some protection on the future use of their farm. Farmers may also receive tax benefits if they work with a land trust to sell their farm at a somewhat lower price, and the trust arranges for easements to be established on the farmland. Also, because the farm value is permanently restricted to agricultural use, it should qualify for a lower property tax.

Shared Equity Mortgages

Some land trusts have a special emphasis on helping beginning farmers gain access to farm ownership. One tool they use is a shared equity mortgage. This arrangement allows a beginning farmer to move into farm ownership without having to assume the full capital costs of farm financing all at once, and may sharply reduce or eliminate the need for a down payment.

In a typical shared equity mortgage a land trust will provide part of the farm purchase cost (using their own funds or the value of a donation from the retiring farmer), and will hold an equity share in the farm for that amount. This equity share is usually tied specifically to the land and not the farm buildings or home, so that all increases in value of these buildings will stay with the farmer. The beginning farmer retains all farm management responsibilities, and obtains conventional mortgage financing for the remainder of the farm purchase. The land trust may work with the farmer's lender to subordinate their equity share in place of a down payment by the beginning farmer.

In establishing a shared equity agreement, the beginning farmer and the land trust will negotiate specific provisions to allow the farmer to buy out part or all of the equity share at some future date. This will include provisions on how to allocate any increase in land values if the farm is resold to another party, and an agreement to transfer part of the equity share to the farmer in exchange for establishing conservation easements on the farm.

Sale of Conservation Easements

In some cases, land trusts may be able to purchase conservation easements from farmers. For example, in areas facing serious pressure from development, a land trust may negotiate with a farmer to purchase an easement that would restrict future development and keep the land in farming. A similar easement could be used to protect an important natural area on a farm. In areas where development pressure has pushed land values beyond the level that a beginning farmer can afford, the sale of these easements may allow a retiring farmer to receive full market value for his/her farm, but still sell it to a beginning farmer (with conservation easements attached) at the agricultural value. This may also reduce the property taxes on the farm.

This strategy is used frequently in states such as Vermont where there are special state programs to provide funding to land trusts for easement purchases. In Wisconsin, these programs are still in the discussion stages. However, some land trusts or local governments may have access to their own financing sources, and the Wisconsin Stewardship Fund is able to provide funds for the purchase of easements that protect important natural areas.

Tax Reduction Strategies

There are several ways in which land trusts can provide tax benefits to retiring farmers, and in which these savings can be used to make the farm more affordable for a beginning farmer. In some cases, a retiring farmer may choose voluntarily to donate a conservation easement to a land trust. If the easement meets the federal tax code requirements for land conservation, the value of this donation may be considered as a tax

deduction to offset income. For many farmers who have built up substantial equity in their farm, this tax deduction may allow them to sell their farm at a lower price and still receive a net income that is comparable to a market sale.

Farmers may also work more directly with a land trust to sell their farm and protect its agricultural use in the future. A farmer may negotiate a sale of the farm to a land trust for a price that is somewhat below the full market price, with a stipulation that the trust will establish conservation easements on the farm and will seek to sell the farm to a qualified beginning farmer. In legal terms this is called a “bargain sale” and the farmer will be able to consider the difference between the full market price and the sale price as a tax deduction. Again, by using this strategy, and avoiding some of the sale and transaction costs in a conventional sale, the farmer may be able to receive a net return that is comparable to a market sale. At the same time, the land trust has increased flexibility in working with a beginning farmer to buy the farm and in establishing protective easements on it.

Shared Equity Mortgage Beginning Farmers

One of the most effective ways that a land trust can work with a beginning farmer is the use of a shared equity mortgage. In negotiating either the purchase of a conservation easement or a bargain sale with a retiring farmer, a land trust will end up holding some equity or value in the farm. The use of a shared equity mortgage can allow the land trust to use this equity in a way that both makes it easier for a beginning farmer to obtain financing to buy the farm, and secures the long-term public benefit in land conservation.

In essence, the land trust will identify a potential buyer for the farm who is comfortable with the need to observe the conservation easements that have been placed on the land. In most cases these easements will require provisions similar to the Wisconsin Farmland Preservation Program and basic ASCS farm management plans. The land trust will then set a price on the farm that is consistent with appraised

value, and will negotiate a purchase agreement with the beginning farmer that provides for the land trust to hold an equity share in the farm that is consistent with either the retiring farmer’s contribution or the amount of the easement purchase. The beginning farmer will then obtain a conventional mortgage to finance the remainder of the farm cost. In many cases, the land trust may be able to negotiate an agreement with the lender to consider its equity share in lieu of all or part of the down payment requirement for the beginning farmer.

The shared equity agreement provides clear provisions for how and when the beginning farmers can buy out the land trust’s equity at some future date. This financing model may allow beginning farmers with limited equity a better opportunity to move into farm ownership. It may also lower down payment requirements, lower debt payments during the critical first years, and allow beginning farmers to target their limited resources toward other aspects of the farm plan.

Example

The following is an example of a farm sale and shared equity financing plan that was developed for a retiring and beginning farmer in Wisconsin.

The retiring farmers wanted the farm to stay in farming and to be sold to a beginning farmer, but they also wanted to cash out and not use a land contract. They were having difficulty finding a buyer who could qualify for financing. The appraised value of the farm was set at \$150,000. The land trust provided a professional evaluation of the farmer’s net after-tax return based on a market sale at \$140,000 for the farm and \$100,000 for the chattel. After allowing for depreciation, exclusions, fees and taxes, it was estimated that this farmer’s net return would be approximately \$198,000. The land trust also offered an analysis of a bargain sale at \$110,000 with a \$40,000 tax deduction. It was estimated that the net after-tax income would be approximately \$194,000

In this example, the land trust was able to propose a farm sale to the retiring farmer that was close to the return they would get on a market sale. They were also able to propose a

farm purchase to a beginning farmer where they would hold an equity share of approximately \$40,000, the beginner would have a mortgage of \$110,000 and a basic conservation easement would be established. In this case, a local bank agreed to consider the land trust's 26 percent equity share in lieu of a down payment by the beginning farmer.

Summing Up

Knowing what options are available with regard to sale, purchase, or transfer of a farm is the first step in analyzing the alternative that's best for you, whether you are a beginning or a retiring farmer.

Planning for the Four D's

Planners often identify four major events that can severely impact a farm family or a family business: death, disability, disaster, divorce—the Four D's. Often in the enthusiasm, hope, and excitement that accompanies the establishment, expansion or transfer of a business to the next generation, we forget that even the best-laid plans do not always work out. Even though it may be difficult to discuss negative issues such as death, disability, disaster and divorce it is important that you take the time to discuss the implications of these issues and how to handle them if necessary. We are all aware that we cannot control the future or plan for every eventuality; however, the decision to begin or retire from farming is a major life decision. By taking the time to consider and make provision for events which could ultimately destroy the farm business or carefully thought out farm transfer, we can ultimately increase the likelihood of success for the future of the operation.

Planning a farm transfer without providing protection against the possibility of any one of these major events is gambling with your future and your family's future, whether you are entering or exiting the farming business.

Some questions you need to consider are:

- What if someone dies?
- What if someone is disabled?
- What if there is a disaster?
- What if there is a divorce?

How you answer these questions and how you arrange for dealing with the possibility of any of them will depend on how you believe they may impact the farm operation. Can the operation survive, for example, if either spouse dies? What if the spouse who dies is not actively employed in the operation but works and has benefits such as health insurance to protect the family? What if the person providing the major labor and/or management dies or is disabled or incapacitated for a prolonged period of time? How long a period of disability can the operation survive? Should there be life insurance? Should there be disability or income continuation insurance to cover the major contributors? How can we protect assets from becoming part of a divorce settlement? How much crop insurance, liability insurance, casualty coverage is needed and can the farm afford it? How will a major illness or injury affect the operation? Do we have enough health insurance to avoid an impact on the business finances in the event of a major illness or injury?

Marital Property

Wisconsin is a marital property state. This means that each spouse has certain rights to property regardless of whose name is on the property. As an example, income and any benefits associated with income earned by either spouse during the marriage, as well as income earned during the marriage from any investments, is considered marital property.

Individual property is property owned by an individual prior to marriage, property designated by written agreement as individual property, and property received by gift or inheritance.

In the event married partners wish to keep any individual property, they must take affirmative steps to do so. A written property agreement between the parties, executed either prior to or during the marriage is the best protection for parties who want to designate ownership interests in property. These agreements are especially important when a family business such as a farm is involved.

The Mixing Rule Marital Property

Failure to keep good records to assure that individual property is kept separate can lead to application of the “mixing rule.” Under this rule, if marital property is mixed with a non-marital component and the non-marital portion cannot be segregated or traced, the entire asset becomes marital property. Of course, none of this may matter if the parties remain alive, happily married and in a viable farming operation.

Survivorship Marital Property

Designation of property as survivorship marital property accomplishes several goals. First, upon the death of the first spouse, survivorship marital property passes automatically to the surviving spouse without having to go through probate. Second, the surviving spouse gets a “stepped-up basis” on all of the property, not just the “half” belonging to the deceased spouse. This increase in basis allows the surviving spouse to dispose of the property without having to pay significant capital gains tax.

More and more couples are using marital property agreements. The agreements can be used to set forth an understanding in writing of who owns what property; who has the right to manage certain property; how income will be treated, how financial obligations brought into the marriage will be paid, and how assets brought into the marriage or acquired by gift or inheritance will be classified.

Couples who have children from a prior marriage, who have substantial assets or debts to bring into a marriage, or couples who will be participating in risky business operations (like farming) have special reasons to consider entering into a marital or pre-nuptial agreement. Leaving such important issues to chance may well mean that the best plans and the best intentions will not be enough to protect each party’s interest in the event that things don’t work out.

I believe you can’t afford to make payments of more than 30 percent of your milk checks—these should always be 20 percent for family expenses and 10 percent for unforeseen things. Always put aside extra money.

Delores Brey

Boy, that 10 percent got shot this year—we’ve had some big expenses—\$12,000 for fertilizer, buying corn, fixing the well, a compressor, a tractor transmission to be replaced. But—we haven’t had to borrow money—yet. I’m proud of that.

Bev Brey

I tell Bev that they have to reinvest their money in something else besides agriculture. So many farmers have put all their money back into the farm, and that’s a mistake. IRA’s are great tools for farmers.

Delores Brey

farm life

I've made it very clear to my children that we're not leaving anything. I'm going to use what money we've got. We earned it. We had nothing served to us on a silver platter. Still, I know what we need to be comfortable. We don't want to make a pile of money at our kids' expense.

Delores Brey

I feel everyone should have universal life. For farmers, especially young farmers, additional term insurance is called for to protect the other spouse "in case." For me, I'd further my schooling and discontinue farming (if something happened to Mark). You need enough money to keep you going through that time. Think and plan ahead.

Bev Brey

Estate Planning

Having a marital property agreement gives you the foundation you need to develop other plans for the disposition of your estate. Several documents are key in any estate plan: these include a will, durable power of attorney, and power of attorney for health care. In addition, you may want to establish a trust for a variety of reasons. It is important to seek competent advice from an attorney who understands the needs to protect both the operation and transfer of a farm business.

Most of us don't like to think about death; however, it is important to consider the implications of death on the farm business to make appropriate decisions for the long term good of the farm business. When beginning a farm business or transferring one it is a good idea to consider how an estate plan might benefit the business operation. What happens if I'm not here tomorrow? How would my absence affect the business? Who is depending on me? Are my affairs in order? These are questions that need to be asked and answered by all parties before completing any farm transfer.

Once the plans have been made, don't forget to revisit them on occasion. Things change, children are born or adopted, become adults, and marry. The needs of your family will change during each stage of your life. Make sure that your estate plan changes with your family.

Protecting the Business,

Life itself is a risk. We all know that it will end sometime. And farming is undeniably a risky business. It is subject to the weather, fluctuating markets, changing consumer demands, rising costs of production, and the uncertain cost of money. Farm families need to consider how to minimize their risks in order to assure that the business will remain viable and the family will not be destitute in the event of a death, disaster, disability, or divorce.

Life insurance can provide protection for families and/or the farm business in the event of the death of one of the owners. For young families who generally have higher debt and less cash to work with, term life insurance may offer an attractive, low cost

alternative to whole life or other investment protection. Term policies do not have a value except upon the death of the insured.

Providing for income protection is important to protect a farm business if one of the key parties becomes temporarily or permanently disabled. Disability or income continuation insurance can provide the dollars to cover family living or hired labor expenses during the period of disability. Farming is not only a risky business, it is a dangerous occupation. Farm accidents and farm related illnesses affect thousands of farm families annually. Farming is categorized as the single most dangerous occupation in the United States. Given these facts, it's important to take affirmative action to minimize risks to the family and the business.

Insurance coverage can be purchased to cover you in the event of disability or death. But an equally important step is looking at all aspects of your farm operation. Identify any areas of risk and establish plans to reduce risk by education. Prevention of accidents and farm-related illnesses should be one of the key goals for any farm business. Begin with a thorough review of the farming operations, farm tasks, farm machinery and equipment, farm buildings, electrical service, watering systems, well, septic system, and farm topography. Even routine tasks should be analyzed to ensure that safety is built into every aspect of the operation. We have all heard of the expression "an accident waiting to happen." Using appropriate safety procedures and being alert to your surroundings will help you and your family avoid potential hazards and take action to mitigate harmful situations. This type of "insurance" is one of the best protections you can have for your farming operation.

Disaster

When we hear the word "disaster," we generally think of natural disasters like a tornado, drought, or flood. A broader definition could include any major event or circumstance which has a severe impact on the farming operation. These might include stray voltage, a serious disease problem within a dairy herd, contaminated feed or contaminate water supply, all of which can put the operation into a financial tailspin.

The United States Department of Agriculture (USDA) has been the agency to provide disaster assistance to farmers who experience crop losses due to disaster. In the past, disaster benefits have been available to eligible farmers whether or not they were program participants and whether or not they were covered by crop insurance. In part because of significant costs to the federal government due to disasters of recent years and in part due to the pressure to cut costs for USDA programs, eligibility for disaster payments has been changing in recent years. In more recent disaster programs eligibility has been contingent on the applicant being in compliance with other program requirements (for example: compliance with conservation program regulations) whether the farmer was a participant in those other programs or not.

Although disaster programs have never provided full coverage for the losses farmers received the trend has been to further limit eligibility. It is important to keep up to date regarding changes in the disaster and insurance programs and planning for how your operation will adjust to them as they are established.

Analysis, mitigation, and prevention are the best insurance against disasters such as stray voltage and water contamination. A farm's electrical, water and waste disposal systems as well as everything mechanical should be checked by certified professionals prior to purchase. Thereafter, systems should be checked on a regular basis. Farmers also need to watch for any changes in the behavior of their livestock or in production so that corrective action can be taken immediately.

Because a disaster can have such a sudden and severe impact on a farm business, it's important to consider both insurance and prevention avenues available for your farming operation. Additionally, when at all possible, you should set aside savings or other nonfarm investments that can be available to you in the event of a disaster.

Divorce

This topic is covered last because it is an issue most people find hard to discuss in advance. We know death is inevitable. But divorce is something people prefer not to plan

for. Yet, we know that as many as one out of two marriages ends in divorce. Coupled with the high stress level of farming today, the potential for divorce cannot be ignored. Facing the possibility up front can alleviate some of the uncertainty in the farming business in the event of a divorce.

Earlier, we discussed the importance of having a marital property agreement that lists all assets and debts as well as all ownership and management responsibilities. You should be aware, however, that even with a marital property agreement, divorce property division rules allow the court to consider whether the terms of the agreement will result in an inequitable property division. The court can also declare the marital property agreement as it pertains to divorce unenforceable. Generally if the agreement has been carefully considered prior to signing, if both parties have had adequate representation, and if the agreement seems to treat both parties equitably the court will look more favorable on the agreement. It is critical that any marital property agreement be reviewed by a separate attorney for each party prior to signing.

Planning, Planning, Planning

The best way to prepare for a farm transfer is with thorough and proper planning. Open discussion and goal setting are important components of thorough planning. But no transfer operation can be fully planned without discussing and addressing the possibility of death, disability, disaster, or divorce. While you may not be able to avoid any of the Four D's, proper planning may help minimize their impact on the transfer process and may prevent breakdown of the transfer arrangement and/or loss of the farm. Make sure the professionals you work with to put together your transfer plan consider options for handling the Four D's.

Finally, like all farm transfer plans, plans for addressing the Four D's should be reviewed and updated on a periodic basis.

Chapter 5 Financial Considerations

Your Lender and You A Farmer's Perspective

A discussion of money, bankers, and other lenders, communication, respect, honesty, trust, commitment and other virtues which come in handy when asking for a loan.

As most of us know, it's very difficult to begin a business of any kind without some serious amount of financial strength up front, at the beginning. There are those of us who wish to begin farming who will have the help of a parent or other relative or business associate, and who won't need to go to the financial markets to obtain money for pursuing the dream. And to those we say, "Good, we're happy for you!"

But if you will need to borrow money to begin, it is beneficial to have an understanding of the relationship between you and the lender.

The first thing to understand is that the lender is in business to serve the financial needs of the community within which it is located. It wants to loan money. That is its business. And it wants the borrower to be able to and willing to repay the loan. The task of judging whether the loan applicant is able to and willing to repay the loan falls under the term *risk assessment*.

Risk assessment is an attempt to judge the veracity, honesty, personality, business acumen, past accomplishment, and future potential of the loan applicant's probability of being able to do what he or she says will be done in relation to the use and repayment of the funding being requested.

It behooves the loan applicant, then, to be punctual, respectful (spit out the Copenhagen before going in the office—take off your seed corn baseball hat), and complete the information you wish to convey to the loan officer. Make sure you look like the person you want to be seen as.

A complete and accurate proposal will help the loan officer fully understand your application. Come in prepared with a current balance sheet, 3 years of historical cash flows

or a realistic projected cash flow and a logical game plan.

You should have a list of three or four personal references who can speak favorably to your character and past performance. It is helpful also to have a list of three or four businesses with which you have done business in the past so that the loan officer can check out your track record.

Because in this publication we are speaking mostly of entering farmers and their financial needs, we will contain the discussion to that end, although much of what is said here can also apply to short term financial needs for any farm operation.

If you are a beginning farmer, you should know that a priority is that you convince your lender that you know your business and that you understand the costs of doing business—both short term and long term costs—as well as fixed and variable costs.

The best way for you to relate these costs is with the use of a **pro forma statement**. This is a numerical depiction of what the business will look like as a year goes by. It includes a **cash flow statement** as well as a reflection of other capital assets and liabilities (or what you think the balance sheet will look like).

In the beginning, a basic cash flow statement can be developed using the IRS schedule F form which is used to report the cost of doing business on a farm. It will help you make sure you do not miss any costs which will be incurred as the year goes by. It is best to include a separate sheet illustrating the logic of how you came up with large expense items such as feed and labor expenses.

You should also be prepared to list **all** your assets, as the lender will need to understand what collateral will be available to protect the lending institution in the case of default. Put **everything** down. The balance sheet is not a collateral statement, but it shows what you have earned in assets so far in your life. This is a pure form of risk assessment. But beyond that, you should know what return on *your* investment you are dreaming of—oh, I mean figuring on! And in order to calculate

farm life

You can raise the corn and buy the pig and make money, or you can buy the corn and raise the pig and make money, but you can't buy the corn and buy the pig and make money.

Anonymous

this on your pro forma statement, you must have a list of and the value of all your assets.

The pro forma statement should look like a **profit and loss statement and a balance sheet** for the first year of your prospective business—by the month. Most county extension agents and CPA's can provide you with examples of these documents as well as good guesses as to what the cost of veterinary expense is per cow or fertilizer cost per acre, and other information which will help you understand the total cost of doing business in the area in which you anticipate going into farming. Make sure that **you understand** the information. Don't just have someone else fill it out and just drop it on the banker's desk. **You need to be able to answer the banker's questions.**

Keep in mind that you will have to use a figure from somewhere to calculate return or income, and in the case of dairy this is the price of milk per hundred weight. **Be conservative** in your estimates in this area—or you may not be able to perform as desired and may not be able to repay your loan as promised.

Make sure that your projected borrowed dollars includes at least six weeks of operating money. It will take that long to get the first milkcheck. You don't want to start your new business out by owing your suppliers money.

The balance sheet portion of the pro forma statement will also allow you to estimate the return on your investment as well as other financial ratios, such as short term liabilities to variable assets—or those assets which can be liquidated quickly to cover debt repayment.

The following analogy may enhance your understanding of those ratio relationships. Think of the balance sheet as a cookie jar where your net worth is stored. The cash flow is a mixing bowl where expenses and income mix and then net income is drawn out. Imagine an exchange tube that runs from the mixing bowl to the cookie jar. When you make a profit, net income flows from the mixing bowl to the cookie jar. But, the reverse is also true. When there is not enough profit or net income generated in the cash flow (mixing bowl), net worth is pulled

out of the balance sheet (cookie jar) and net worth drops. This is caused by a build-up in supplier payables or perhaps borrowing more money to operate. Net worth **must** grow every year.

A most valuable ratio is one that compares your debt to your total assets; in other words, for each dollar of asset you own, how many dollars of debt do you owe? The lender will want to know that you have invested significantly in the business and that you aren't trying to buy the pig and the corn. Generally, you will be able to borrow 70% of what you need to buy your assets. This means that you will have to provide a 30% down payment using your own money that you have saved. If your lender works with you to secure a Farm Service Agency (FSA) guaranteed loan, you may be able to borrow 90% of the money with only a 10% down payment. FSA also offers direct loans that can be as high as 100% of needed money with a \$200,000 limit.

Though we should not stretch the discussion of lender relationship too far, it is possible to calculate the size of an anticipated dairy business by understanding that a cow requires about four percent of her body weight each day in dry matter intake and that grain concentrate is typically fed at a rate of one pound of concentrate for each three pounds of milk given. These relationships, along with the knowledge that it usually requires fifty-five to sixty percent of the gross income to produce the milk, allows us to know how much money we will have left over for living expense—return to labor and management.

In the 1980's the operating expense rate on dairy farms was 50% of the gross income. That allowed a 50% cushion for other items to be purchased. In the 2000's the rate of expenses is 70 – 80% of the gross income. This makes operating very tight and there is no longer a "cash cushion". Health insurance alone can run \$1,000 per month. Other operating and living expenses continue to increase. But, unfortunately, the price of milk and other commodities is at the same level that it was in 1980!

If you assign a figure for living expenses at \$20-25,000 per year or \$30-40,000 per year

you then have all the numbers necessary to calculate how many cows you would have to milk to have a viable dairy business.

How big must the farm be? The average livestock unit requires three tillable acres. It is not the size of the farm that is as important as the profitability of the farm. Your expected life style and return on your investment must also be factored in ahead of time. The size of the farm or number of cows milked must reflect your expectations. In today's economy many cash flows will show that it takes 75 cows per family to make a dairy operation work.

Most agricultural enterprises are becoming very specialized and specific. Make sure that you have selected a lending organization that understands the business that you are in. You also need to make sure that the loan officer you are working with is knowledgeable about your business.

The reason for going through this analysis is that you must remember that debt repayment is in three parts:

- Interest
- Principal
- Taxes; income taxes

Many people forget that principal repayment is an after-tax activity. While interest expense is tax deductible, principal repayment is not. You will pay income tax on the earned money that is used to pay the principal payment and there is no place to deduct it on your income tax form. Therefore, the cost of the money is not just the loan interest paid to the bank, but also the income tax that you will have to bear prior to paying the principal back. Make sure that you expect to have a profitable farm that will generate adequate income to necessitate paying taxes. Some farmers manage their farms so they don't have to pay taxes. You will never make money by trying to minimize the IRS payments.

One further point; it may seem that with the non-cash flow tax deduction of depreciation, you are *not* paying tax on the principal repayment amount in the early years of the loan. In other words there are times when you can repay principal and not pay taxes, but the depreciation expense is to be used for

farm life

Without dreams, there is no reason to work—and without work, there is no reason to dream.

upgrading your capital requirements, buying machinery or making long term investments in your capital plant (barn, sheds, etc.). Farmers have been known to make their loan payments regularly and still go broke because they couldn't replace the machinery that was worn out in five to seven years.

These issues illustrate how valuable a balance sheet is to the success of an operation. It allows you to list all your assets and liabilities, and list the assets at their fair market price (how much would they bring if you were to have an auction today?). This analysis allows you to know if your assets are making you a profit so that you are, in fact, replacing them as required and you can upgrade when needed or desired. The balance sheet must grow beyond the depreciation that you take. A **growing balance sheet** shows that you are making real financial headway.

The development of the balance sheet and profit and loss pro forma statement will force you to consider these points **prior** to going to the bank for the loan. By demonstrating to the lender that you understand the business you want to be in, you greatly increase the chances of a favorable decision on your loan application.

Finally, remember that the lending institution, after granting the loan, has become a member of your business team (sometimes it seems almost a member of the family) and as such, your loan officer deserves to be kept abreast of any significant changes which may take place in the business. Changes in the business may strongly impact the lender's risk exposure. Be open and honest, share your plans and objectives and goals. Invite the loan officer to visit the farm and see what you are doing with their money. Agriculture is a capital intensive business. Very few people have the means to enter into production agriculture without having to borrow money. Borrowing money is okay. You must use other people's money to make your own money. Provide a profit and loss statement and a balance sheet to the lending institution at least annually, with an oral review in between. A lender is not there to micro manage your business. The lender is there to provide money for additional capital that you need, but don't

have, which is important in running your farm. Keep your lender in the loop. Do not pester them but let them know of your progress and any plans of change. Lenders do not like surprises. Let them know in advance of your needs.

And hire a tax professional to figure your taxes. It's hard enough to keep up with advances in farming without having to keep up with changes in tax law. Depending on the size of your farm you may need to hire an accounting firm to prepare monthly or quarterly profit and loss statements. As tight as margins are today, fast adjustments are important if something is going wrong. If you only do a profit and loss statement once a year, you may be out of business and not know it.

Your Lender and You: A Lender's Perspective

Entering or Exiting?

In any farm transaction, **family** is the place to start, not finances. Some families feel that all members should be treated equally when the farm is transferred. Remember, sons and daughters who are working off the farm are making their own money in their jobs. They have 401Ks, earn vacation time and are developing a viable career. Those who stay on the farm are putting in their time as "sweat equity". Their reward includes extra assets in the farm. But if there's one son or daughter who has worked on the farm for several years and has been the only one to get it to succeed, problems are likely to arise. That child is not going to think it's fair for the others to have any "say" in the business. Making it harder for some families will be the fact that the highest and best value for that farm may not be as a farm, and it may not stay in the family. It may make more financial sense for a family to sell the farm **not** as a farm, but as something else.

There are advantages to inter-family transfers. You avoid the instability that might occur if you have to rent a farm from a stranger, who can raise the rent on you every year. Parents can gift the machinery to a child, and use creative strategies in renting the land and renting or selling the cows. Of course, a lot of unrelated people make these arrangements work too. In family transfers

the sellers need to be very close to being debt free or have a healthy net worth. There is only room for one banker in a dairy operation. Sellers must let go! Buyers must take responsibility.

In either case, inter-family or non-family transfers, the retiring party has to ask: "How committed is the purchaser to running that farm so there is cash flow?" The beginners have to ask: "How committed is the seller to helping me succeed?" Parents should start in early years sharing balance sheets and cash flows as part of the learning process. It is too late to wait for the day that the farm is transferred.

In any transfer situation, the farm has to "pull the deal". It has to cash flow. If the farm is to be transferred, the young couple needs income to live and operate the farm, and the retiring couple needs to retire comfortably. There are lots of farms out there that can't provide for both parties.

Getting into Farming

If you're planning to work with, or take over from your parents, start with the tax returns. Know what that farm is making and figure out how you can improve on the numbers, either by cutting costs or by increasing productivity. Generating extra gross income is even more important than cutting expenses. Work toward getting debts paid down, at least keep them no higher than a certain percentage of total assets.

Take debt on incrementally, then add on to it as you build net worth. Building that net worth is a matter of replacing capital with labor—in other words, hard work. If you're not committed early, you won't build capital. Commit first, and enjoy life later. Your parents took 30 years to build their net worth. Don't expect to have everything that they have your first year. Make sure that you come to the farm with an attitude of "patience".

Young people especially need to pick their priorities carefully. There are some young people who want the \$30,000 pickup but don't have any earning assets. Some young farmers are overly optimistic. They may want the niceties of the wage earners, but fail to

realize that the farm can not support those things in the early years.

The farm has to cover principal, interest, family living, and some money to set aside for improvements. Some family living expenses that many young farmers overlook or forget are hired labor and life and health insurance. These two are musts these days, and so is some form of retirement **other** than the farm, like an individual retirement account. And they have to put something into that account every year.

Farming is a business of slowly building of net worth—through a lot of sacrifice. If you're not willing to sacrifice in your earlier years, it won't work. I urge young people to work real hard at first so they can get their debt reduced and build their net worth. How do people get to be doctors and lawyers? Through hard work and sacrifice up front, and their education.

Farming isn't merely a matter of milking cows and working hard any more. It's knowledge too. A lot of young farmers get right out of high school and go into farming. That's fine to go without formal education, but you'd better commit yourself to education and training on an ongoing basis.

Farm Service Agency Beginning Farmer Program

Probably the greatest challenge to preserving the American family farm is locating viable farm families to replace the generation of farmers before them. A program called The Beginning Farmer and Rancher Program takes an important step by providing the financing necessary for a person to venture into farming. The Beginning Farmer and Rancher Program is administered through the United States Department of Agriculture's (USDA) rural lending agency, the Farm Service Agency (FSA).

Participants in the Beginning Farmer and Rancher Program must meet the requirements for a typical FSA farm borrower, plus other requirements specific to this program.

The program is divided into the two general categories of **Operating** and **Ownership**. Both categories are designed to help farmers get started in farming and then to eventually

cut off their dependency on the federal government.

A beginning farmer or rancher is an individual who (1) has not operated a farm or ranch for more than 10 years; (2) meets the loan eligibility requirements of the program to which he/she is applying; (3) substantially participates in the operation; and, (4) for ownership loan purposes, does not own a farm greater than 30 percent of the average size farm in the county. All farm ownership loan applicants must have participated in the business operation of a farm for at least 3 years.

The person must have a viable five-year plan of operation with all non-farm income used only for family living. The operating loan would be made with a seven-year term and the recipient would be expected to graduate into commercial lending circles within a ten-year period. The interest rates on the loan would be either regular FSA rates for operating loans or a reduced rate for people qualifying for Limited Resource Interest Rates.

Beginning Farmer Farm Ownership Loans are geared to smaller farm operations and may not be used to purchase farms where the purchase price or appraised value exceeds \$250,000. The applicant must have 10 percent of the purchase price for a cash down payment. The next 50 percent may be financed through another lender with terms of at least 30 years. The remaining 40 percent of the purchase price can be financed through the FSA at a 4 percent interest rate for a fifteen-year term. If a Beginning Farmer Operating Loan has been secured, the applicant cannot obtain a Beginning Farmer Farm Ownership Loan until the applicant has been farming for five or more years.

The Farm Services Agency makes money available to beginning farmers in two ways. FSA can make a direct loan to the farmer and/or can guarantee a loan to the farmer through another institution. This arrangement makes it possible for FSA to be directly involved with financing 90 percent of the purchase price of a farm for a beginning farmer. Forty percent would be a direct loan and fifty percent would be a guaranteed loan through another lender.

Wisconsin Housing and Economic Development Authority (WHEDA)

Beginning Farmer Bond Program

Wisconsin's Beginning Farmer Bond Program authorizes the issuance of \$10 million in federal tax-exempt bonds. The program is designed to assist qualified first-time farmers acquire agricultural property using private sector conventional loans carrying interest rates lower than prevailing rates. Administration of the program is through the Wisconsin Housing and Economic Development Authority (WHEDA).

Eligibility

Financing can be provided by a variety of entities including lending institutions, individuals, partnerships, corporations, limited liability companies, and others. The lender is issued a bond which exempts payment of federal income tax on the interest income received from the loan issued to the beginning farmer. The lender's tax savings is then passed on to the farmer in the form of a lowered interest rate for the full term of the loan. Generally, that rate reduction ranges between 2 and 3 percentage points. When the lender is a bank, each bond adds credit to that bank's Community Reinvestment Act portfolio.

To be program-eligible, the beginning farmer must not ever have held a direct or indirect ownership interest in **substantial** farmland. Substantial is defined as having a fair market value more than \$125,000 **and** an acreage more than 30 percent of the median farm size in the county targeted. The county-by-county list follows this article.

In addition, the farmer must be a Wisconsin resident, at least 18 years of age, with a net worth of no more than \$250,000. Adequate farming knowledge and working capital, as well as access to equipment, are each vital. Beginning farmers must not only actively participate in the operation and thus be the principal user(s) of the investment, they must also demonstrate that **the operation will become their primary livelihood**.

Speculative and/or hobby applicants are not program-eligible.

Once it appears an applicant is program-eligible, the next step is to link up with whoever is willing to provide the financing:

- the lender, who assumes 100 percent of the risk involved, will perform the credit evaluation, and
- the application must be completed and submitted to WHEDA jointly by the applicant and the lender.

Uses

The WHEDA Beginning Farmer Bond (BFB) can be used to purchase farmland with or without buildings. Beginning Farmer Bonds can also be used for farm improvements on the purchased farmland, for example: barns, sheds, silos, bins, grain dryers, workshops, milking parlors, permanent fences, wells, terraces, conservation ponds and waterways, irrigation systems.

Beginning Farmer Bonds can be used to purchase depreciable agricultural personal property, for example, TMR mixers, bulk tanks, milking equipment, breeding livestock, tractors, combines, tillage and harvest machinery, wagons, trucks, pickups. These bonds can also be used to purchase a **combination** of listed types of real and personal property.

But, remember that **neither** real nor personal property can be purchased with Beginning Farmers Bonds **if** the beginning farmer applicant already owns a **substantial** amount of farmland before making an initial application.

The beginning farmer may not use Beginning Farmer Bonds for more than a lifetime aggregate of \$250,000—farmland, improvements on that farmland, and new or used depreciable personal property. Of the possible \$250,000, no more than \$62,500 can be for "used" property. Used property includes used machinery and female animals used for breeding purposes. Open or bred heifers, gilts or lambs are considered "new" property, not subject to the \$62,500 minimum. For Beginning Farmers Bond purposes, all farmland, including any **existing** improvements, is considered "new."

Restrictions

Of course, there are restrictions. Beginning Farmer Bonds can only be held by a non-related third party. Therefore, a farmer cannot sell the farm to any party by utilizing a land contract. Land contracts can be

attractive from the seller point of view because they allow for capital gains on principal to be taxed over the term of the contract rather than all at once as in an outright sale. Related party sales can utilize the Beginning Farmer Bond program if they are outright sales **and** the selling party does not retain a “financial interest” in the operation after the sale. The law requires that lenders who make loans to finance related party sales to provide appropriate notice to borrowers of the restrictions and that the bond proceeds may not be re-transferred from sellers to purchasers as part of efforts to transfer both property financed with the bond proceeds and the bond proceeds received by the seller.

Example: Son wants to buy the family farm from Dad. He can use Beginning Farmer Bond financing if he borrows the money from the bank and pays cash to Dad for the purchase. Dad cannot turn around and transfer the cash back to the son. Congress specifically did not want such “step transactions” to be allowed with Beginning Farmer Bond financing. The bank collects interest on the loan and that interest is exempt from federal income tax. Because of the exemption, the bank may even be able to give the son a break on interest. That can be negotiated between the son (borrower) and the bank (lender). Dad, though, may be on the hook for some capital gains taxes. Careful planning with a tax expert will be required before a farm transfer takes place.

Beginning Farmer Bonds cannot be used to finance the personal farmhouse if it has a value greater than 3 percent of the farm transaction. However, in most situations, that limitation is **not a real obstacle** inasmuch as there is very little 100 percent financing. Therefore, in most situations, the cash down payment can be allocated to cover the dwelling value with the balance of the purchase financed with an Beginning Farmer Bond.

Also, Beginning Farmer Bonds cannot be used for working-capital loans nor can they be used to refinance existing debt.

To avoid potential problems, beginning farmers and their lenders are jointly urged to

contact WHEDA **before** commencing any intended financial actions and/or contracts.

FSA and WHEDA - Together

Beginning Farmer Bonds can be used to piggy-back with a Farm Services Agency **Beginning Farmer Downpayment Loan**. It could work like this: The FSA-qualified beginning farmer would make a 10 percent cash downpayment on the first-time farm. At the same time, FSA would provide a subordinated loan at a 4 percent interest rate for 30 percent of the farm’s cost. The remaining 60 percent of the loan package would then be made with private financing at a negotiated interest rate. Beginning Farmer Bonds could be used to attach to that 60 percent amount, reducing the interest rate on that portion, thus resulting in an attractive blended rate of interest. Interested beginning farmers must contact FSA first when such a loan combination is desired.

Costs

WHEDA’s administrative costs are covered by borrower fees. The lender pays WHEDA and is then entitled to collect from the farmer. A \$100 nonrefundable application fee must be submitted with the application. In addition, a fee of 1.5 percent of the amount of the loan must be paid at the time the loan is actually made. The 1.5 percent fee may be financed with loan proceeds—amortized over the life of the loan contract if so desired.

Summary

Beginning Farmers Bonds have been administered in some states for more than a decade. They work!

For example, Illinois has issued Beginning Farmer Bonds, sometimes called Aggie Bonds, to 3,139 beginning farmers for a total of \$337.8 million with a default rate of under 2 percent. In 2002 the Iowa program helped 136 beginning farmers with a total of \$18.4 million.”

Wisconsin has issued 57 loans since it began in 1994, for a total of \$8.2 million.

For further information on Wisconsin Beginning Farmer Bond program, contact WHEDA at 1-800-334-6873.

Beginning Farmer Program Median Farm Size

County	Median Farm Size (Acres)	30% of Median Farm Size	County	Median Farm Size (Acres)	30% of Median Farm Size
Adams	270	81	Marathon	200	60
Ashland	255	76	Marinette	215	65
Barron	230	69	Marquette	267	80
Bayfield	216	65	Milwaukee	60	18
Brown	162	49	Monroe	180	54
Buffalo	300	90	Oconto	210	63
Burnett	224	67	Oneida	122	37
Calumet	195	59	Outagamie	195	59
Chippewa	237	71	Ozaukee	189	57
Clark	200	60	Pepin	260	78
Columbia	189	57	Pierce	200	60
Crawford	216	65	Polk	209	63
Dane	172	52	Portage	220	66
Dodge	195	59	Price	200	60
Door	160	48	Racine	171	51
Douglas	165	50	Richland	238	71
Dunn	230	69	Rock	170	51
Eau Claire	186	56	Rusk	241	72
Florence	200	60	St Croix	200	60
Fond du Lac	190	57	Sauk	207	62
Forest	200	60	Sawyer	201	60
Grant	240	72	Shawano	200	60
Green	210	63	Sheboygan	190	57
Green Lake	205	62	Taylor	240	72
Iowa	240	72	Trempealeau	240	72
Iron	180	54	Vernon	160	48
Jackson	240	72	Vilas	100	30
Jefferson	145	44	Walworth	192	58
Juneau	211	63	Washburn	250	75
Kenosha	158	47	Washington	153	46
Kewaunee	171	51	Waukesha	148	44
La Crosse	211	63	Waupaca	184	56
Lafayette	251	75	Waushara	210	63
Langlade	240	72	Winnebago	196	59
Lincoln	200	60	Wood	170	51
Manitowoc	196	59	Menomonie*	200	60

*Menomonie County is counted in Shawano County

Alternative Models

Land Contracts

A land contract is a permanent transfer of real estate where the seller provides financing to the purchaser over the duration of the contract. Both parties to the contract are bound by the terms specified. If one party fails to perform, then the other party can take legal action to recover damages.

Purchasers are the owners in all respects except they generally do not hold title until all conditions of the contract are met. All income generated on the farm belongs to the purchaser. All expenses are the responsibility of the purchaser, including property taxes and insurance on the buildings.

Both parties need competent legal advice before entering into a land contract. The seller needs expert tax advice because often there is a major income tax liability generated by the sale. The purchaser needs to consider the financial consequences of a purchase to be certain there is adequate cash flow to make all payments and meet other financial obligations.

The two parties need to negotiate the terms of the land contract. There is a lot of flexibility for both parties in drafting the agreement. At a minimum, a land contract for sale should include the following items:

- The purchase price, amount of down payment, principal payment requirements including dates of payment, duration of contract, and interest rates to apply. Generally the down payment is between 10 to 30 percent of the contract price. If principal is not completely amortized over the life of the contract, the balloon payment could be refinanced from other sources or rolled over into another land contract. The seller needs to comply with minimum interest to avoid possible adverse income tax consequences under imputed interest rules.
- The date of possession.
- How the property tax bill for the year of sale should be split.
- How government payment or rent due are to be split.

- A complete legal description.
- Any rights to be reserved by the seller.
- Any easements that exist should be stated.
- Any property to be removed by the seller.
- Date the title is to be transferred to purchaser. Normally this is transferred only after all payments have been made.
- Any restrictions on prepayment or amount of principal payments in any one year.
- Insurance on buildings to be carried by the purchaser and what happens in the case buildings are destroyed (a new building must be constructed or the insurance proceeds go to seller).

The major benefit to the seller is to spread the capital gains over several years and have reduced tax liability. It also provides retirement income and does not affect social security benefits. The seller may get a higher interest rate through the land contract than alternative ways of investing the funds.

The major risk for the seller is that the purchaser will default on payments and the seller will get the farm back with buildings in poor condition and soil fertility depleted, resulting in a lower value for the property. This can also be a problem for the seller if the payments are a source of retirement income. In the event the purchaser stops making payments the seller gets the farm back and keeps all prior payments, but this may take several years and cause considerable legal costs.

For the purchaser, the benefits are lower down payments and a lower interest rate than could be obtained from other lenders. There may be flexibility in payments if allowed by the contract. The biggest problem for the purchaser will be cash flowing the farm operation to make the payments. This is especially true when the down payment is very small.

- During a five year period running from 2003 through 2008, Wisconsin will be one of five states participating in a pilot program through Farm Service Agency. During this pilot program period, each participating state FSA office will guarantee five land contracts each year. If this pilot is successful, the program may be available in the future.

Check with your county or state FSA office for an update on this pilot program.

Shared Mortgage Agreement

This type of debt instrument is a deviation from the standard mortgage. The shared mortgage agreement provides for a sharing of any increase in value of the real estate between the owner-borrower and secured lender. Normally the owner-borrower receives all the increase in value of the property. Under the shared mortgage agreement, the owner-borrower benefits in one of two possible ways in exchange for sharing gains in real estate values. One is a reduced interest rate that would be paid under the shared mortgage agreement compared to the standard mortgage. Shared mortgage agreements are often used when the lender restructures the debt by writing down part of the debt obligation. Under the second arrangement, the lender writes down the debt, but in exchange expects any gain in value of the property to be shared.

With the shared mortgage agreement a valuation is made at the initiation of the contract and at some future date as called for in the contract. Any increase in property values during the intervening time is shared in some percentage between the lender and borrower. Quite often it is a 50/50 sharing but it could be a different percentage. The lender's share of the augmented value could result in either the amount added to the debt or the lender would have an equity interest in the property until the time the property was sold.

Land Trusts

In a land trust the land owner transfers property to a trust. The trustee owns and manages the property. The powers of ownership and control are governed by a trust agreement. By having the trustee owning and managing the property, the

beneficiaries are left with a personal property interest only. There are a number of distinct advantages to this trust. When there are multiple owners, property interests can be transferred easily between the owners. Probate can be avoided upon the death of an owner. The trust property of the deceased passes according to the trust terms.

Seller Financing Options

There are a number of options available in which the seller is involved in helping finance the sale of farm assets. These methods are described in more detail in other sections.

They include:

- **Land Contracts:** a very common way to finance the sale of a farm to another party where the seller provides financing for the purchaser.
- **Installment Sales:** includes land contracts but can also encompass personal property. The seller provides the financing and is paid over a period of years.
- **Mortgage:** property is sold and the party selling takes a mortgage similar to that of a traditional lender in providing financing.
- **Land Trust:** property is transferred to a trustee for management. Equity interest in property can change without complicated changes in title.
- **Lease Agreements with Purchase Option:** lease payments are received over the life of the lease with the purchaser having the option to purchase the assets at the end of the lease contract.

Sweat Equity Agreements

In this agreement ownership interest is gained in exchange for labor input. The actual method may take a variety of forms. The most usual is that one receives a share of the income in the business in exchange for labor contributions. The amount of income received is based on the labor contribution relative to the total contributions from all resources. Generally, the labor contribution receives high priority in determining all contributions in order to get a young person into the farm operation.

An individual may start as an employee with part of the compensation being made in commodities such as livestock. Over time, the young person builds equity interest in the farm.

There are other situations where parents are willing to make gifts to the younger generation to augment their ownership interest. This may well be justified if in the past the younger person helped build equity on the farm but received low wages.

The exact form of the property accumulation makes little difference as long as all parties agree with the technique for building ownership interest for the younger generation.

Sweat equity is a way to build ownership interest without the risk of debt and associated financial risk. The major problem is that it is a slow process to build much equity.

Lease with Option to Buy

An Option Contract is an agreement in which the owner of the property agrees to sell the property at a fixed price or determinable price at some future time. A fixed price could be the fair market value as of the date of the agreement. Any increases in value would benefit the potential purchaser. Another option would be to state the process for determining the price as of the date the option is exercised. The method of appraisal used and/or who would do the appraisal could be stated in the option.

Terms of the option must be stated. If payment is made in installments, then interest rate, payment dates, amount of payments, security, and terms for default need to be stated.

The date of execution for the option must be stated. The potential buyer must pay some reasonable compensation for the option. The option must be an arms-length deal. There must be some specific date or event that terminates the option.

Installment Purchases

Purchases of personal property can be financed by the seller. Machinery or livestock can be acquired and paid for over a number of years.

An installment purchase is distinct from a lease/purchase agreement. An installment purchase results in payments being applied to principal payment and interest. The interest portion of payments is a deductible business expense for the purchaser.

There may be some adverse tax consequences for the seller. It is best to seek tax counsel before making an installment sale. The gains are normally prorated over the period of principal payments. For example, if ten percent of the contract price is paid in one year, the seller will pay capital gains tax on that portion received.

The sale of machinery, equipment and certain other assets can result in adverse tax consequences. If there is gain due to depreciation, the gain is treated like ordinary income and is entirely taxable in the year of sale regardless of when payments are received. If the capital gain is less than the depreciation claimed then the gain due to depreciation is ordinary income taxed immediately and the remaining gain is installment gain over the life of the contract. Another problem arises when debt is transferred with assets. If the debt exceeds the tax basis then all the gain is in the year of sale. This could occur with the sale of raised dairy cattle which have a zero tax basis and debt transferred as well. It is even possible that more tax will be due than the seller receives in payments in the year of sale.

To plan ways to minimize adverse tax consequences of an installment sale, see your tax planner prior to finalizing the agreement.

Chapter 6

Economic Feasibility

This manual has emphasized family goal setting and planning, noting that beginning farmers must understand and reconcile conflicting goals within the family and between the entering and exiting families. In Chapter 2, Roger Williams reinforced the importance of thinking ahead: “. . . each family should give careful attention to their wants and needs. . . . Younger farmers are increasingly seeking some assurance that there will be adequate money to support living expenses . . . seeking some things previous generations did not have: time off and money for vacations, fun activities, home improvements . . . Increasingly spouse’s and children’s needs are being considered and increasingly spouses from nonfarm families don’t support the concept of delaying gratification until retirement . . . What are your monthly needs for family income right now? . . . How will they change as children get older? . . . Is the farm you are considering economically viable? . . . Can it produce the income you need to cover farm expenses, meet your current needs for family income, and allow you to meet the evolving needs of farm and family?”

We continue to stress the need for planning and goal-setting in this chapter, focusing on financial expectations and realities.

Individuals and families that are potential farm entrants need first to clearly identify their individual and family goals. They must recognize that the retiring farmer, whether a family member or not, has goals that compete with theirs. But, most important, before making the purchase decision, the potential entrant must look the resource requirements and income generating ability of the farm squarely in the eye and answer these questions: Can the beginning farmer generate sufficient net cash flow to:

- Maintain an adequate standard of family living?
- Make timely principal payments on debt?
- Replace depreciable farm capital?
- Accumulate surplus to invest in the expansion of the farm business or to enhance family living standards?

I can say without conceit that this farm would not have been successful without my financial management. But, I wouldn't have had any money to manage without my husband's hard work and good farm management.

Delores Brey

The Supply of Farming Opportunities

While we hear about young people who would like to become farmers, what is the supply of viable farming opportunities in Wisconsin?

The age distribution of Wisconsin farmers might suggest that there will shortly be a large supply of farming opportunities in Wisconsin. There is a relatively large number of Wisconsin farmers age 55 and older who will reach retirement age during the next decade, thereby providing farming opportunities for new entrants. However, this may not be the case, for two reasons.

First, farmers may reduce the scale of their farm business and shift to less labor-demanding crops and livestock as they approach retirement but continue to farm. For example, there were 29,637 Wisconsin farmers in 1982 who were age 55 and older. Ten years later, the count of those that were age 65 and older (ten years older) was 42 percent of that number. Although they were age 65 or older, 12,742 Wisconsin farmers continued to farm, including over 7,000 who were in their seventies. While this net change in farm numbers hides the dynamics of farm entry, farm exit, and death, it signals that retirement age is an individual choice for farmers that is not readily predicted by chronological age.

The second reason that the age distribution of Wisconsin farmers may not be a good predictor of the supply of new farming opportunities relates to the capacity of existing farms to generate viable net income for prospective new entrants. While a farm business may provide an acceptable level of income for the retiring farm family, it may fall far short of meeting the needs of a farming entrant. This is because a) the older couple may be debt free, (like more than 30 percent of Wisconsin farmers) and not obligated to meet interest and principal payments out of farm earnings, b) the retiring farmer can "use up" the capital invested in machinery, equipment, and buildings while the younger farmer will continually need to replace and update them to maintain the long-term productivity of the farm business, and c) the draw on the farm's income for consumption by an older couple with no dependent children will be less than what will be needed

to meet the expectations for an adequate standard of living by a younger couple with children.

Adequate Standard of Living

How much net farm income is needed to attain an adequate standard of living? This will vary among couples, affected in part by what they can earn in nonfarm employment and the intensity of their ties to farming or to a particular farm.

A starting point for developing a dollar benchmark for adequate income can be found in the federal guidelines developed to mark the minimum level of income at which our society is willing to have its poorest members live. Those poverty threshold income standards are calculated to include only the cost of food plus other bare necessities for families of different ages and sizes. For a family of four, the current poverty threshold is \$18,400 per year. Purchasing health insurance will require an additional eight to ten thousand dollars of income above the poverty threshold. In other words, poverty level consumption plus buying health insurance would require about \$26,000 to \$28,000 per year.

Aspiring to earn poverty level income as a farming goal may not seem acceptable for a young family considering becoming farm entrants, but twice that level, or about \$36,200 for a family of four, may be a more appropriate target. That is still below average family income in the United States. Earning \$36,200 would place the potential farm entrant in the lower one-third of the family income distribution in this country.

The standard of living issue may be complicated somewhat by there being a dwelling on the farm for use by the beginning farmer, either as a tenant or new owner. Ownership and operating costs of that dwelling (e.g., real estate taxes, utilities) are family living expenses for the farmer, just as they are for an urban resident. They are not farm business expenses, although in practice the distinction may become blurred.

An Example of a Farmer Near-Retirement

What resources are needed for a potential farm entrant to get started and to earn

acceptable income? The resources and historic earnings record of the farm under consideration should be examined carefully by the potential farm entrant. For an example of the process, we turn to the past farm records and performance of a representative Wisconsin dairy farm for which that information is documented. The differences in the contribution of the farm business to family income for an established farmer on that farm compared with a prospective entrant will be illustrated.

The dairy enterprise on our example farm is characterized by a stanchion barn, three upright silos, and a somewhat above-average level of mechanization. There are 125 crop acres owned, plus 55 rented that support a 45-cow dairy herd plus slightly more dairy young stock. The dairy herd averages 19,500 pounds of milk per cow and crop yields are above average for the neighborhood.

The dairy farm in our example can be viewed as typical, or at least not unusual for Wisconsin. Assets at fair market value are as follows: feed and supplies \$30,000; livestock \$90,000; machinery and equipment \$80,000; and land and buildings \$200,000, for a total of \$400,000. The current (near retirement) operator has no debts. The total assets and their distribution among asset classifications are similar to those of the 605 farmers with comparable herd size in the report, "Balance Sheet of Wisconsin Dairy Farms - 2000", by Gary Frank of the Center for Dairy Profitability. In 2000, they averaged \$450,500 in assets and \$102,800 of debt.

Gross revenue (cash farm income) on our example farm is \$126,200 and cash farm expenses are \$68,250 for a net income of \$57,950. For the operator and spouse (no dependents) that income more than meets their estimated consumption needs of \$25,200. For the Wisconsin farmers with similar herd size the gross revenue was \$120,880. With cash farm expenses of \$74,950, this left a net cash income of \$45,930. That is, our example farm is of similar size but generates greater net cash returns than the comparable farms. An entrant on this farm would have the advantage of taking over an above average farm.

The Issue

The farm generates a good living for the current operator and spouse. Will it also cover the financial needs of a farm entrant? If the current owner can be matched with a well-trained, knowledgeable farm entrant and if the current owner provides seller financing, can a successful farm exit—farm entry transfer take place?

Seller Financed Transfer

In the first example in Table 1, the owner offers to sell this complete farm business to a prospective farm entrant at its fair market value (\$400,000) on an owner-financed land contract paying 6 percent interest, requiring \$50,000 down payment and \$10,000 annual principal payment. The prospective farm entrant has sufficient financial assets to make the down payment but must pay current operating expenses, interest, principal payments, and family living expenses from the milk check.

The current, retiring farm operator is a good dairyman with a good herd, is well-mechanized, and generates above average production from his dairy herd and for his crops. Gross revenue of \$126,200 minus \$68,250 cash farm expenses gives a net income of \$57,950. This leaves a residual that is ample to meet estimated consumption needs (about \$25,200) plus \$32,750 for additional investment, retirement planning, or enhanced consumption (Column 1, Table 1).

When the farm is transferred, it is likely (though not certain) that the new entrant will initially experience decreased productivity levels. That is because the new operator will begin management of a new dairy herd and start farming new lands without prior knowledge of their unique characteristics. In our example, however, we assumed that production and gross receipts were unchanged (Column 2, Table 1). Cash expenses were increased by \$21,000 (\$350,000 debt at 6 percent interest) and this decreased net cash farm income to \$36,950. That net covers principal payment on debt (\$10,000) and replacement of farm machinery and equipment (\$11,250).

The residual of \$15,700 remaining for family living consumption is below the federal

poverty level income threshold for a family of four (\$18,400). That residual can be increased if the seller is willing to charge less than market rates in a seller-subsidized transfer.

Seller Financed Subsidized Transfer

If, for example, the seller charged 4 percent interest instead of 6 percent as in the preceding example, the residual remaining for the farm entrants would be about \$22,700. That would allow consumption at about the poverty threshold level plus being able to contribute towards the purchase of health insurance (Column 3, Table 1).

By reducing the interest rate from 6 to 4 percent the seller would forego \$7,000 in interest income. For the seller to maintain their former level of consumption (\$25,200 per year) the required principal payment would need to be increased by \$1,200 per year.

Alternatively, or in combination with below-market interest rates, the seller might charge below-market prices or give assets to the entrant. For example, machinery might be sold at the seller's undepreciated remaining cost (book value) rather than fair market value. Feed on hand when the entrant takes over, silage or hay for example, might be given to the entrant, etc. Such gifts reduce the amount of debt for the entrant and thus the interest obligations.

The Internal Revenue Service (IRS) may, for tax purposes, view loans made to family members at below market interest rates as income and as gifts. In general, the dollar value of the difference between the interest rate charged and the market rate may be taxed as if it were income received by the seller and taxed as a gift by the recipient. The IRS market rates can change monthly; therefore, the tax implications of such transactions should be explored in advance.

This illustration shows that intergenerational farm transfers, as well as farm transfers between unrelated parties, may involve terms that are less than the market rates. The selling price of the farm assets or the interest rate may be reduced to assist the younger generation begin farming and become

established. Seller and buyer may have some shared goals, such as keeping the family farm in the family for another generation, or keeping a well-established herd or farm business in operation. However, equity issues with nonfarming children and goal conflicts between generations may also be present (see Chapter 2).

Federal Assistance Program (FSA)

Federal assistance programs have been developed to help beginning farmers finance their activities, and several states have or are developing financial aid programs. Federal assistance is contained in the Agricultural Credit Improvement Act that was recently implemented and is administered by the Farm Service Agency (FSA). Two FSA programs are illustrated here (Column 4, Table 1).

In the example, the FSA Operating Loan Program is used to obtain \$200,000 in a direct loan for operating credit and equipment at 5 percent interest amortized and repaid in 10 years. This requires an annual payment of \$25,900, of which \$10,000 would be interest the first year.

Second, the FSA Down Payment Loan Program is used to fund 10 percent of the purchase price of the farm land (\$40,000 loan) at 4 percent interest amortized over 15 years. The annual payment is \$3,600, of which \$1,600 is interest the first year.

The remaining \$110,000 of the debt is seller-financed at 6 percent interest, requiring payment of \$6,600 interest plus \$2,990 in principal the first year.

Compared with seller financing, there would be lower interest but higher principal payments. The net effect is a residual for family living consumption that is below the poverty threshold (Column 4, Table 1).

Renting Land and Machinery

As a third alternative, consider the outcome if the farm entrant purchases only the feed and cattle from the current owner and rents the machinery, land and buildings (Column 5, Table 1). Total debt would be \$70,000, interest the first year would be \$4,200, and with a four-year repayment schedule, annual principal payments would be \$16,000.

Unlike land leases, there are few traditions or precedents for writing farm machinery rental agreements, but there are many opportunities for misunderstandings. In our example, the current owner continues to pay for repairs and maintenance, but does not replace machinery or equipment as it wears out or becomes obsolete. The entrant in effect begins to invest \$11,250 per year in a new set of machinery. Property taxes would be the responsibility of the current owner, not the entrant.

This is an improvement over the other unsubsidized alternatives, but it still leaves a residual only slightly above the poverty income threshold.

Improving Efficiency or Expanding the Farm Business

In the example given above, the farm entrant took over an existing farm business that was above average in production and financial returns. However, on other farms there may be profitable opportunities for an entrant to increase the output from the farm or expand the farm business. The costs, expected returns, credit needs, and the probability of successfully exploiting these opportunities need to be budgeted in advance.

For example, expanding the dairy herd on the example farm would involve acquiring additional cropland or buying feed. It would mean remodeling the existing stanchion barn or building a new facility. The expansion issue involves the impact of such a long-term commitment of family labor and financial resources on other, nonfarming goals of the family.

Off-Farm Employment

Prospective farm entrants may have access to income sources other than the farm business. Almost all farm families have some nonfarm income sources, and nonfarm sources make up the major portion of farm family income in Wisconsin and the nation.

While once viewed as a transition phase into or out of farming, the nonfarm employment of farm operators and spouses has emerged as a widely adopted method used by farm families in Wisconsin and the nation to help meet their financial goals. Off-farm employment in

many cases includes family coverage under a health insurance plan, which in itself may be worth several thousand dollars as a fringe benefit.

While the labor distribution on some types of farms is such that it is possible for both the operator and spouse to hold off-farm jobs, that generally does not work well on dairy farms. One skilled adult must be in charge on the farm full-time, but off-farm work by the other adults present is possible on dairy farms. The income from off-farm work, less the cost of any additional hired labor to replace that person, can be used to augment the residual available for family living consumption in any of the examples in table 1.

Hired Farm Worker

The prospective farm entrant in our example held a small amount of net worth relative to the total assets of the farm business, but did hold a different valuable resource—farming skills and the ability to do farm work. That mix of resources might be used to purchase an undivided share of the total farm business plus work on that farm as a hired farm worker.

In our example, the \$50,000 in net worth held by the prospective farm entrant could purchase about 13 percent interest in the total farm business. Wages would be negotiated between the seller and the entrant. If the entrant's share of profits plus the wages received covered family living expenses, the residual could be used to purchase a larger share of the farm business from the senior partner.

Rural Nonfarming Alternatives

For at least five decades there have been more children in farm families than the number of realistic, acceptable farming opportunities. This circumstance is likely to persist, even though recent decades have shown reduced numbers of farm-reared young persons relative to the number of farms.

A “right to farm” does not exist any more than there is a right to enter any other occupation, e.g., to be a NBA basketball player, to be a brain surgeon, or to be an agricultural economist. In each case, the

human and financial resources available to the individual must be compared with the resources demanded by the occupation, and a conclusion drawn about the likely outcome. If the demands of the occupation and the resources available by an individual do not match, then alternative careers should be explored.

Both the federal and state government at times offer job training programs directed at limited resource farmers, dislocated farmers, and first-time farmers. Job training and other vocational assistance is available in some locations for farmers who decide to change occupations.

There are many agriculturally related occupations, and in some, farm-reared youth have an advantage over other candidates. If a rural or small town place of residence is important, that can be consistent with a wide variety of nonagricultural occupations. There are three times as many nonfarm self-employed persons in rural counties as there are self-employed farmers. So it is not necessary to become a farmer to achieve the independence of self employment in a rural area.

Additional References

U.S. Department of Commerce, Bureau of the Census. *1992 Census of Agriculture AC92-A-49*. Volume 1, Geographic Area Series, Part 49, Wisconsin State and County Data. Superintendent of Documents, U.S. Government Printing Office, Washington, D.C. 20402.

Table 1.
Financial Comparison of a Retiring Farm Owner Versus a New Farm Entrant
Operating the Identical Farm Business

	Retiring Farm Owner (1)	Seller Financed (6%) (2)	Seller Financed (4%) (3)	FSA & Seller Financed (4)	Rent Land and Machinery (5)	Your Estimate (6)
Assets and Debts:						
Assets						
Feed &	\$ 30,000	\$ 30,000	\$ 30,000	\$ 30,000	\$30,000	
Livestock	90,000	90,000	90,000	90,000	90,000	
Machinery & equipment	80,000	80,000	80,000	80,000	0	
Land & buildings	200,000	200,000	200,000	200,000	0	
Total Assets	\$400,00	\$400,000	\$400,000	\$400,000	\$120,000	
Debts:						
Non – gov.	\$ 0	\$350,000	\$350,000	\$ 110,000	\$ 70,000	
Gov. lenders	0	0	0	240,000	0	
Total Debt	\$ 0	\$350,000	\$350,000	\$350,000	\$ 70,000	
<i>Net Worth</i>	<i>\$400,000</i>	<i>\$ 50,000</i>	<i>\$ 50,000</i>	<i>\$ 50,000</i>	<i>\$ 50,000</i>	
Farm						
Cash Farm						
Milk sales	\$103,910	\$103,910	\$103,910	\$103,910	\$103,910	
Livestock	18,810	18,810	18,810	18,810	18,810	
Other farm	3,480	3,480	3,480	3,480	3,480	
Total	\$126,20	\$126,200	\$126,200	\$126,200	\$126,200	
Cash Farm Expenses:						
Interest	\$ 0	\$ 21,000	\$ 14,000	\$ 18,200	\$ 4,200	
Property tax	5,830	5,830	5,830	5,830	0	
Machinery	0	0	0	0	11,250	
Land rent	2,810	2,810	2,810	2,810	13,000	
Other cash farm expenses	59,610	59,610	59,610	56,610	50,975	
Total	\$ 68,250	\$ 89,250	\$ 82,250	\$ 83,450	\$ 79,425	
<i>Net Cash Farm Income</i>	<i>\$ 57,950</i>	<i>\$ 36,950</i>	<i>\$ 43,950</i>	<i>\$ 42,750</i>	<i>\$ 46,775</i>	
Financial Obligations:						
Principal Pmt. on Debt	\$ 0	\$ 10,000	\$ 11,200	\$ 20,890	\$ 16,000	
Farm Capital Replacement	\$ 0	\$ 11,250	\$ 11,250	\$ 11,250	\$ 11,250	
Residual available for family living consumption & investment	\$ 57,950	\$ 15,700	\$ 21,500	\$ 10,610	\$ 19,525	

We know people that buy things just to avoid paying income tax. That will get you in the end, because you still have to pay it back. You do that a lot and you end up paying more interest on the stuff you bought (to avoid tax) than you would pay in income tax. Besides, what is so bad about paying income tax in a great country like ours?

Delores Brey

Chapter 7 Legal & Tax Consequences for Farmers

Overview

Legal and tax planning is important in any transaction, whether one is a beginning or exiting farmer. Legal planning primarily consists of placing everyone's understanding in writing to protect each individual's interest and to resolve any uncertainty or misunderstanding at a later date. Information contained in the various legal documents can provide the basis for how an item is treated for income tax purposes, thus having an impact on your tax planning.

Tax planning is the process of structuring a transaction in a way that will reduce one's tax liability. This reduction in tax liability is attained by the timing of a transaction or in the method of reporting the transaction. Some decisions will subject the transaction to immediate taxation; other transactions may allow for deferral of tax to a later date. For example, a taxpayer may decide to postpone the sale of an item until the following year because tax rates will be lower at that time.

As a basis for tax planning, a number of points need to be reviewed. First, taxpayers are required to account for their income annually. For most people, a calendar year beginning January 1 and running through December 31 is the appropriate tax period. In some cases, a fiscal year may be used. Second, **tax planning cannot be done solely because of the impact the transaction has on one's taxes.**

The economic feasibility of a transaction should be reviewed before completing the transaction. All too often, the economic feasibility or other concerns may be overlooked for the sole purpose of obtaining a tax deduction. Keep in mind that tax laws continue to change; there are changes in the federal income tax system every year. This means farmers need to be alert to tax changes and the possible need to revise their business plans to maximize tax advantages.

The Importance of Tax Planning

To help in understanding the importance of tax planning for both beginners and exiters, we will begin by discussing the tax impact for an individual who is leaving or exiting farming.

Once a beginner understands the needs and requirements of the exiting farmer, he or she will better understand how to approach tax planning as a beginning farmer.

Exiting farmers have always been considered “land rich and cash poor.” Each farmer, after a number of years on the farm, has put a good amount of sweat equity into the entity, usually with land values appreciating. Additional money may or may not have been put away for retirement purposes. Therefore, it is essential for an exiting farmer to try to get the best price for everything he or she has

Case 1A: Sell All Assets in Year 1

Assumptions: Married filing jointly, family of four
Income before sale of farm: \$30,000

NOTE: Income taxes calculated using 2002 tax rates

in order to put away a nest egg for retirement. To accomplish this goal, many exiting farmers sell everything at one time in order to get the best price. This in turn, can have an adverse tax impact on the intended nest egg. If an exiting farmer were to sell the entire farm in the same tax year, a number of adverse tax consequences may follow.

The adverse tax consequences arise primarily from the bunching of income in the year of sale. Since our income tax system imposes a higher rate of tax on income in higher tax brackets, the bunching of income causes the income to be taxed at a higher rate. To illustrate the effect of bunching, we will begin with an example of a farm family that sells all the farm assets in one year and will show the taxes that can be saved by spreading out the sale of the assets over two or more years.

Item	FMV	Basis	Gain
50 Cows	\$ 50,000.00	\$ 0.00	\$ 50,000.00
50 Heifers	\$ 25,000.00	\$ 0.00	\$ 25,000.00
Machinery	\$ 80,000.00	\$ 20,000.00	\$ 60,000.00
Real Estate	\$ 200,000.00	\$ 50,000.00	\$ 150,000.00
Additional Taxable Income		\$ 285,000.00	
Additional Income Tax		\$ 64,166.00	

This example shows that the sale of the farm increased the family’s income taxes by more than \$64,166.00 for the year of sale.

Methods of Minimizing Income Taxes

Several income tax planning methods can be used to minimize the income taxes that must be paid on the sale of the farm. These methods can be used in a variety of combinations.

Sell Assets Over a Period of Several Years

A simple method of reducing income taxes is to spread the sale of assets over more than one year. The effect is to move some of the income from the higher income tax bracket into a lower income tax bracket. To illustrate, assume the family in Case 1A sold all of the farm assets except the land in year one and sold land in year two. The effect, as shown in Case 1B below, is to reduce the income taxes on sale of the farm assets from \$64,166 to \$52,153—a savings of \$12,013.

**Case 1B: Sell cows, heifers and machinery in Year 1.
Sell land in Year 2**

Assumptions: Married filing jointly, family of four
Income before sale of farm: \$30,000
Income taxes calculated using 2002 tax rates

Year 1 Sales			
Item	FMV	Basis	Gain
50 Cows	\$50,000.00	\$ 0.00	\$ 50,000.00
50 Heifers	\$ 25,000.00	\$ 0.00	\$ 25,000.00
Machinery	\$ 80,000.00	\$ 20,000.00	\$ 60,000.00
Additional Taxable Income		\$ 135,000.00	
Additional Income Tax		\$ 25,521.00	
Year 2 Sales			
Item	FMV	Basis	Gain
Real Estate	\$ 200,000.00	\$ 50,000.00	\$ 150,000.00
Additional Taxable Income		\$ 150,000.00	
Additional Income Tax		\$ 26,632.00	
Total Additional Income Tax		\$ 52,153.00	

If the asset sale can be spread over more than two years, the income taxes can be reduced even further. For example, if the family in Case 1A could sell the cows and machinery in year one, and sell the heifers as springing heifers in years two and three and then sell the land in a later year, they could reduce the income taxes on sale of the farm assets to \$50,531—a savings of \$13,635.

Case 1C: Sell cows and machinery in Year 1;

Sell heifers in Year 2 and Year 3;

Sell land in later year

Assumptions: Married filing jointly, family of four

Income before sale of farm: \$30,000

Income taxes calculated using 2002 tax rates

Year 1 Sales			
Item	FMV	Basis	Gain
50 Cows	\$50,000.00	\$ 0.00	\$ 50,000.00
Machinery	\$80,000.00	\$20,000.00	\$ 60,000.00
Additional Taxable Income		\$110,000.00	
Additional Income Tax		\$ 19,363.00	
Year 2 Sales			
Item	FMV	Basis	Gain
25 Heifers	\$12,500	\$ 0.00	\$12,500.00
Additional Taxable Income		\$12,500.00	
Additional Income Tax		\$ 2,268.00	
Year 3 Sales			
Item	FMV	Basis	Gain
25 Heifers	\$12,500.00	\$ 0.00	\$12,500.00
Additional Taxable Income		\$12,500.00	
Additional Income Tax		\$ 2,268.00	
Later Sale			
Item	FMV	Basis	Gain
Real Estate	\$200,000.00	\$50,000.00	\$150,000.00
Additional Taxable Income		\$150,000.00	
Additional Income Tax		\$ 26,632.00	
Total Additional Income Tax		\$ 50,531.00	

Installment Sales

The income taxes from the sale of some assets can be reduced by using the installment method of reporting. That method allows the seller to report the gain from the sale as the payments are received. Consequently, the income is spread over several years and allows it to be reported in a lower income tax bracket.

To illustrate, assume the family in Case 1A sold the cows and machinery in year one, the heifers in years two and three, and entered into a ten-year installment sale of the farm in year four. As shown in Case ID below, this method of selling the assets reduced the income taxes on the sales to \$26,117 - a savings of \$38,049.

**Case 1D: Sell cows and machinery in Year 1;
Sell heifers in Year 2 and Year 3;
Sell land in year 4 on a 10 year installment contract.**

Assumptions: Married filing jointly, family of four
Income before sale of farm: \$30,000
Income taxes calculated using 2002 tax rates

Year 1 Sales				
	Item	FMV	Basis	Gain
	50 Cows	\$ 50,000.00	\$ 0.00	\$ 50,000.00
	Machinery	\$ 80,000.00	\$ 20,000.00	\$ 60,000.00
	Taxable Income		\$ 110,000.00	
	Additional Income Tax		\$ 19,363.00	
Year 2 Sales				
	Item	FMV	Basis	Gain
	25 Heifers	\$ 12,500.00	\$ 0.00	\$ 12,500.00
	Additional Taxable Income			\$ 12,500.00
	Additional Income Tax		\$ 2,268.00	
Year 3 Sales				
	Item	FMV	Basis	Gain
	25 Heifers	\$ 12,500.00	\$ 0.00	\$ 12,500.00
	Additional Taxable Income		\$ 12,500.00	
	Additional Income Tax		\$ 2,268.00	
Year 4 Sales				
	Item	FMV	Basis	Gain
	Real Estate	\$ 200,000.00	\$ 50,000.00	\$ 150,000.00
	Additional Taxable Income		\$ 150,000.00	
	Annual Additional Taxable Income (\$150,000/ 10 yrs)			\$ 15,000.00
	Annual Additional Income Tax			\$ 2,218.00
	Total Additional Income Tax			\$ 26,117.00

For some farmers, it may be more difficult to sell the assets in more than one year. An installment sale of assets that have been depreciated, such as machinery, purchased breeding and dairy livestock, and some buildings, will not qualify for installment reporting since the depreciation recapture rules (I.R.C. §1245 and §1250) require the gain to be reported in the year of sale even if the payments are received in a later year.

If the seller has other income that puts him or her into a higher tax bracket, using the installment method of reporting the gain on sale of land, machinery, and breeding/dairying livestock, will not reduce the total federal incomes taxes paid since the maximum rate on long-term capital gains is 20% (2002). Wisconsin income tax law allows an exclusion for 60 percent of long-term capital gains from income. Therefore, installment reporting will not reduce the total taxes paid for Section 1250 property; it provides a time to obtain monies to pay income taxes.

The income tax rules require the seller to charge a fair market value interest rate on the installment note. The seller or buyer may obtain this fair market interest rate from 2 to 3 local financial institutions. The seller then uses this fair market rate to compute interest to charge the buyer on the outstanding installment note balance.

Gain on Sale of Personal Residence

The Taxpayer Relief Act of 1997 dramatically changed the tax rules governing gain on sale of a personal residence. The new law replaces both the rollover of gain into another residence as well as the once in a lifetime over-age-55 exclusion of up to \$125,000. Under the new law, \$250,000 of gain on sale of a residence (or \$500,000 for a married couple) is not income (and, therefore, not taxed) so long as the residence was owned by and used as the taxpayer's home for at least two of the last five years. Taxpayers can use this provision as often as every two years.

To take advantage of this provision when a farm is sold, the sales price of the personal residence must be separately identified. For purposes of this provision, the personal residence includes the house and the land around the house that is used for personal

rather than business purposes. For example, if a small pasture next to the house is used for pet ponies that are not a part of the farm business, the pasture is included in the value of the personal residence.

Income Tax Basis Adjustment Upon Death

We have often heard the comment that two things in life are certain: death and taxes. Death and taxes are related when it comes to tax planning. For income tax purposes, the basis of an asset is adjusted to the value of the asset on the date of death of the asset's owner. For example, if the owner of the asset has a \$10,000 basis in the asset that is valued at \$15,000 on the taxpayer's date of death, the beneficiary who inherits that asset will have a \$15,000 basis in the asset. If the beneficiary sells the asset for \$15,000, the \$5,000 gain avoids federal and state income taxes.

Some farm families could plan to use this adjustment in basis to reduce the gain reported on the sale of farmland. For example, instead of selling the farmland to the next generation of family farmers and passing the proceeds of the sale through their will, a farm couple may pass the farmland through their will to the next generation.

Generally farm couples may transfer farmland through the will and let the farming child buy the portion of the farm inherited by his or her siblings. We caution farm couples that this places a financial hardship on the farming child's cash flow statement. We advise seeking professional financial analysis before passing farmland through the will to more than one sibling when not all siblings are actively involved in farming.

Avoiding Capital Gains

Since Wisconsin passed the marital property law beginning in 1986, spouses in Wisconsin qualify for the income tax advantage of marital property. For example, if a married couple owns farmland that has an income tax basis of \$100,000 and a fair market value of \$1,000,000 as marital property, when one spouse dies, the basis will be adjusted to the full \$1,000,000 value. The surviving spouse can sell the farmland to the son for the fair market value of \$1,000,000 and incur no

However, once Mark decided he wanted to farm, we sought help from many professionals—accountant, banker, lawyer. The lawyer's first plan really was not fair to the kids, I thought. However, he eventually drew up two options for Mark and Bev to buy. We ended up with a deal where Bev and Mark bought the personal property. They rent the farm from us, with an option to buy in ten years. We gifted the personal property to the kids, which sort of cancels out the interest on the note. They also pay the upkeep. Our banker suggested this approach, because it gave us sufficient retirement income. I called the banker so much about this, he was sick of me! I worked on this for two years.

Delores Brey

capital gains liability. Part of a good estate plan includes a review of how property is held and how ownership may be transferred now to avoid capital gains taxes in the future. By contrast, if the married couple owned the farmland as joint tenants, only the interest that is included in the decedent's estate (usually one-half) will be received on an adjusted basis. Therefore, the survivor would have a basis of \$50,000 in the half he or she owned before death and a basis of \$500,000 in the half received because of his or her spouse's death.

To take advantage of Wisconsin's marital property law, spouses must be sure they own their property as marital property. A formal agreement documents that all property ownership by either spouse is marital property. Upon the farmland owners' request, the County Registrar of Deeds can change the title of the property to marital property.

Transfer of Machinery

Transferring machinery from an exiting to a beginning farmer triggers some of the most difficult income tax issues. Unless the machinery is sold for more than its original purchase price, the gain on the sale of the machinery is treated as ordinary income instead of capital gains because of the I.R.C. §1245 recapture rules. Therefore, the gain does not qualify for the 25 percent federal income tax cap or the 60 percent Wisconsin capital gain exclusion.

If the machinery is leased to the beginning farmer, the exiting farmer is likely to be subject to self-employment taxes as well as income taxes and possibly sales taxes on the lease payments. This applies to machinery with less than 100% of farm use such as all-terrain vehicles, lawn mowers, and office equipment. The rental income may also reduce the social security benefits received by taxpayers under age 70.

If the beginning farmer has an option to buy the machinery at the end of the lease, the IRS can treat the transaction as an installment sale if the purchase price does not reflect the value of the machinery at the time of purchase. The disadvantage of the installment sale method is that the exiting farmer must report all of the depreciation recaptured in the year of sale.

One method of spreading the machinery sales over several years is for the exiting farmer to sell machinery only as it wears out. The beginning farmer buys the replacement machinery. This also helps the cash flow of the beginning farmer by allowing him or her to buy machinery a little at a time.

If the parties are related, the exiting farmer may be willing to give machinery to the beginning farmer. That would eliminate the income tax problem for the exiting farmer.

Gift and Estate Tax Planning

For most Wisconsin farm families, estate taxes are not an issue in farm transfer planning since Congress recently expanded the amount each person can pass on without paying gift or estate taxes. Therefore, we will only briefly discuss two important methods of minimizing estate and gift taxes.

Gift and Estate Tax Exclusion Chart

2003 _____	\$1,000,000
2004 and 2005 _____	\$1,500,000
2006 thru 2008 _____	\$2,000,000
2009 _____	\$3,500,000

2010 Estate Tax Exclusion Repealed 2010 Lifetime Gift Tax Exclusion remains at \$1,000,000.

Make Use of the \$10,000

Gifts up to \$10,000 per year to each donee are not subject to the gift tax rules. Therefore, a taxpayer with an estate worth more than the gift and estate exclusion amount can make gifts of up to \$10,000 to reduce the amount that will be subject to tax. An exiting farmer may use the annual exclusion to make gifts of machinery or other farm assets to be transferred to the beginning farmer.

****Caution: After the date of the gift, when the donee sells machinery, recapture of depreciation may create ordinary income and a taxable transaction.***

Maximize the Benefit of the Gift and Estate Exclusion

Since the gift and estate exclusion applies to both lifetime gifts and transfers at death, exiting farmers can maximize the benefit of the exclusion by using it to give property away before it appreciates in value. Due to

the complicated tax laws, the practice of maximizing the gift and estate exclusion requires a full analysis of the farm couple's health, appreciation of farmland value and future plans of the next generation. In a basic example, assume an exiting farmer is planning to give the farmland to his/her children. Assume the farmland is worth \$600,000 in 2003 and the exiting farmer expects it to be worth \$2,000,000 in 2009. If the exiting farmer initiates the gifting transfer of farmland to his/her children today, the gifted farmland will reduce his/her lifetime gift and estate exclusion from taxes only when the farmland's projected appreciation is less than the estate exclusion, prior to 2010. However, if the farmer's death occurs after 2010, the annual gifting of farmland will create an estate tax liability.

Tax Planning for Beginning Farmers

Beginning farmers usually purchase property in one way or another from an exiting farmer through an intermediary. Keeping in mind the needs of the exiting farmer, the beginning farmer can structure a transaction to the advantage of both parties. For example, in an installment contract, an allocation of the down payment can be made to apply the entire down payment to the purchase of the residence. This allows the seller to take the Section 121 or 1034 election, thereby sheltering most or all of the down payment from taxes. The buyer would then be allowed to use 100 percent of the interest paid as a Schedule F deduction since the debt is all farm debt.

Beginning farmers are usually faced with cash requirements, whether for expansion, updating, or replacing certain items on the farm. In a related party transaction, this need may be reduced or minimized with the items that already exist. However, a beginning farmer going into farming for the first time will need to purchase certain items in order to operate the farm. As a result, the beginning farmer is faced with potentially higher interest expense and cash outlays than the exiting farmer. Therefore, it is essential that the beginning farmer put together a complete budget and cash flow in order to determine what is available to spend on capital items. In fact, it is recommended

that a cushion also be set up in case an emergency occurs regarding the repair or replacement of capital items.

Reducing fluctuations in income can help reduce taxes paid for two reasons. First, the progressive tax rates cause income in high-income years to be taxed at a higher rate. Second, taxpayers cannot take advantage of individual exemptions and deductions available on an annual basis if there is no income for them to offset in the low-income years.

For 2003, there is a personal exemption deduction of \$3,050 for each taxpayer and each dependent. Taxpayers can also take the standard deduction—\$7,950 for joint taxpayers, \$7,000 for heads of households, \$4,750 for single taxpayers, and \$3,975 for married filing separate returns—or itemize if their deductions exceed those amounts. However, if a taxpayer's income is below the sum of these exemptions and deductions, he or she cannot get the benefit of the excess. A married couple with two children has potential exemptions and deductions (in 2003) of $\$7,950 + (4 \times \$3,050)$, or \$20,150. If their income is less than that amount, they cannot use all of those tax benefits.

Example: Assume that Farmer A and Farmer B each file married filing joint tax returns, claim the standard deduction, and each has a total of four personal exemption deductions. As the above example illustrates, you should plan income and expenses to use up at least the standard deduction and personal exemption deduction. If possible, you should also make sure your income does not fluctuate from one bracket to another. Some strategies for evening out your taxable income include the following:

If you are using the cash method, you can postpone selling part of your crop or livestock in a good year, and sell them in a year when prices or sales are down. On the other hand, if you have not had as good a year, you can speed up sales—selling more of your crop and livestock before December 31. You can also delay expenditures or postpone payments, or conversely, buy things before you actually need them, depending upon the net income situation in a particular year. For example, in a year of high gross income you could buy

feed, seed, fertilizer, and repairs—ordinary deductible expenses—even though you will not use them until the following year, subject to I.R.C 464.

However, use this strategy with caution. For the sake of good farm business management, and to satisfy the IRS, there must be some reason for the purchase other than reducing taxes. For example, feed grain is generally cheaper in the fall than in the spring. Therefore, it often makes good business sense for a livestock producer to buy grain before the end of the year. Whether it would pay also depends on prices, storage costs, and the cost of money.

You must make the prepayment for a business purpose—not merely to avoid taxes. That means you should have a reasonable expectation of receiving some business benefit because of the prepayment. Examples of business benefits include fixing maximum prices or locking in a feed supply.

In order to legitimately deduct the cost of fertilizer, feed, chemicals, petroleum, or other annual operation supplies you must pay for them and take possession the year you claim them. They must be bona fide, irrevocable obligations—not advance payments on orders to be placed or on purchases that may be made in the succeeding year.

Plan expenditures for such things as painting buildings, minor repairs or improvements, the purchase of small shop tools, as well as soil and water conservation expenses within limits, so they fall in years of high gross income. This way you may be able to reduce the total taxes paid for the years affected.

You may want to consider incorporating your annual bills such as property taxes into a year when income is high.

Elect accelerated cost recovery depreciation the year you buy an eligible item. This provision allows taxpayers to claim up to \$25,000 of expenditures for capital items to be deducted in the year the item is purchased.

Summary

There are numerous options that exist for a farmer and they can be quite complex. It should be noted that this chapter is not all-inclusive, and it is advisable that before you apply the points discussed above, you should review tax implications with legal counsel and tax experts to see how they apply to your situation.

Chapter 8

Finalizing and Monitoring the Transfer Process

Choosing Your Team

In order to implement your farm transfer plans, you will need the help of a number of experts, including a lawyer, accountant, and lender. You may also need to work with a realtor, a financial consultant, or other professionals to accomplish the goals you have set out for yourself and your family. During the goal-setting and planning process, you may already have identified and used the counsel of your professional team.

Choosing the professionals who will constitute the team of experts to assist you with transfer is an important decision for you. You want to work with professionals who will listen to you and respect and understand the goals you have set out in your transfer plan. Be cautious about professionals who tell you there is only one way to do things, or who tell you that they are the only ones who can provide you with the necessary skills to accomplish your goals. You know what you need. You've done the planning. You've done the analysis. You know what you want. You know what is feasible. Now, you need the people who can put together the necessary documents, counsel you on the process, make sure your interests are protected, give you direction on investments and estate planning, and ways to monitor the transfer to be alert for potential problems. You have the right to feel comfortable with those professionals and you have a right to have confidence that they will provide you with competent service.

When to See a Professional

Some or all of your team may be used during the planning process itself. At a minimum, **no document or contract should be signed by you without consulting with your attorney.** Often, your accountant will also need to give you input prior to entering into an agreement—even a preliminary one.

Because the transfer of a farm is complex, using the expertise of a number of professionals is necessary. It is usually cheaper to spend money to prevent problems

than to spend money to fix problems. If you think about the value of the property being transferred and its importance to your family and your business, several hundred, even several thousand dollars spent to make sure the transfer is properly done is money invested wisely.

If you are not sure whether you need to talk to a lawyer, two services are available to help you. The Wisconsin Farm Center (800-942-2474) provides confidential information and referrals for farmers. General legal information and copies of “A Legal Guide for Wisconsin Farmers” are available through the Farm Center. The State Bar also sponsors a Lawyer Referral Service (800-362-9082) for answering basic legal questions and can refer you to a lawyer in your area who works on transfer and estate planning issues in your area.

Open communication between you and your team is critical to your getting the best and the most in service. Prior to meeting with professionals, get your plans in order, write down questions you have, take with you all your financial, tax, and other papers, and be organized. Preparation for such a meeting will be appreciated by the professional and, in fact, will save you money. Interviewing the professionals to determine if they have the interest, the personality, and the expertise to handle your transfer affairs should be an integral part of the first consultation.

What Will It Cost Me

Members of your team are paid for their professional services. At the first meeting, you should be told what the cost for services will be and how you will be billed. If you're not told, **ask.** Beware of professionals who are unwilling to give you a clear understanding of how much services will cost. Insist on a written agreement regarding your contract with them for services. You need to have an idea of the costs so that you can plan for those expenditures in the transfer process.

Remember, that professional is working for you. If you retain professionals who understand your needs and work with you, you will indeed feel like they are on your team.

Monitoring the Process

Unless you sell your farm outright, you will be involved with the farm process over a period of time. It's important, therefore, that you be prepared to monitor the transfer process. Copies of all your transfer documents, including written goals, plans, cash flows, balance sheet, accounting reports, as well as legal transfer documents should be well organized and available for periodic review.

Remember, these writings are the foundation of your transfer process and can be used to gauge progress, adjust to set backs, or clarify misunderstandings. They should be available

for any meeting between you and the other transfer parties as well as any meetings with your professional team members.

Finally, expect to have to make adjustments. Laws may change which affect the plans you initially developed. Unexpected challenges like injury, death, disability, disaster, and divorce will all require a second look at the transfer plan. Keep in close contact with all your team members and seek counsel whenever a major event occurs which might upset the smooth transition of your farm transfer.

What You Will Need for Your Appointments with Professionals

- ___ 1. A list of farm assets including vehicles, tools, machinery, and livestock. Bring any recent appraisal or loan inventory forms regarding the property.
- ___ 2. A list of personal assets, including savings, other investments, and other businesses.
- ___ 3. A legal description of any real property in which you may have an interest. Your mortgage, abstract, or title insurance policy are good places to look for this information.
- ___ 4. Your complete income tax forms for the last three to five years, including all attachments.
- ___ 5. Copies of the following:
 - a. Financing statements: Register of Deeds or the office of the Secretary of State.
 - b. Security agreements from your file or your lender's file.
 - c. Mortgages, found in your file or your lender's file.
 - d. Contracts, including land contracts.
 - e. Leases or other signed agreements.
 - f. A list of oral agreements you have with a creditor, landlord, tenant or other individuals.
 - g. Financial statements you may have given to anyone in the past two years.
 - h. Written proposal of your transfer plan, including cash flow analysis for the next two to five years, family budget, proposed investments, and complete information about the other family involved in the transfer.
- ___ 6. If you are operating as other than a family farmer or have been a part of any corporation or partnership within the last six years, bring information about that business entity, including tax returns, business books, state and federal tax identification numbers.
- ___ 7. List anyone who owes you money, the amount owed, their names and addresses and how long they have owed you money and why. Bring any supporting documents.
- ___ 8. Bring any marital agreements, or if you have been divorced, a copy of the Judgment.
- ___ 9. List anyone you owe money to, including **relatives**.



Wisconsin Department of Agriculture, Trade & Consumer Protection
 Division of Agricultural Development
 Farm Center
 2811 Agriculture Drive, PO Box 8911
 Madison WI 53708-8911



Farm Link - Senior Farmer Application

This information form is to be completed by prospective participants in Farm Link. Please answer the following questions as completely as possible.

If you have any questions about completing this form, please call 1-800-942-2474

Case Number: _____

Farmer			
LAST NAME:	FIRST NAME	MIDDLE INITIAL	DATE OF BIRTH
ADDRESS:	CITY:	STATE:	ZIP:
HOME PHONE	WORK PHONE:	COUNTY:	# OF CHILDREN LIVING WITH YOU:
CURRENT OCCUPATION	DO YOU PLAN TO CONTINUE IN THIS OCCUPATION? <input type="checkbox"/> YES <input type="checkbox"/> NO		

Describe your educational background and your farm or other work experience:

Spouse/Partner			
LAST NAME:	FIRST NAME	MIDDLE INITIAL	DATE OF BIRTH
ADDRESS:	CITY:	STATE:	ZIP:
CURRENT OCCUPATION	DO YOU PLAN TO CONTINUE IN THIS OCCUPATION? <input type="checkbox"/> YES <input type="checkbox"/> NO		

Describe your educational background and your farm or other work experience:

Please note: The following information is used ONLY to help us match your needs with those of a junior farmer understanding your operation is important in the matching process.

Tell us about your housing situation:			
Is your home located on this farm?	<input type="checkbox"/> Yes <input type="checkbox"/> No	If yes, do you plan to relocate?	<input type="checkbox"/> Yes <input type="checkbox"/> No
If no, when will the home be available?	<input type="checkbox"/> Immediately <input type="checkbox"/> Later, within ___ years		
What alternative housing is available?			

Comments (describe housing — style, size, age, condition, number of bedrooms, type of heat, number of baths):

Tell us about your present operation: Row crop Livestock Other (please specify)

If you raise livestock, please complete the following:

	Number of head per year		Number of head per year
Dairy (No. milking)		Beef background	
Dairy young stock		Beef finishing	
Custom dairy heifers		Farrow-to-finish	
Cow-Calf		Hog finishing	
Other:		Sheep - birth to market	

List the livestock available for the farm transfer (indicate type and numbers, grade or registered):

List the machinery available for the farm transfer (type and condition of major equipment) :

What is the total acreage you control? (own, rent, custom farm, etc.): _____ acres

Total owned	Crop acres	Pasture acres
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Please check your present farming practices (check all that apply):

<input type="checkbox"/> Conventional tillage	<input type="checkbox"/> No-till	<input type="checkbox"/> Sustainable agriculture	<input type="checkbox"/> Strip crop
<input type="checkbox"/> Minimum tillage	<input type="checkbox"/> Ridge-till	<input type="checkbox"/> Organic farming	<input type="checkbox"/> Rotational grazing

Comments:

Describe buildings and facilities that you own or control that might be used as an asset for a potential match. (size, age, capacity, and condition of facilities may be important.)

Livestock facilities: (Dairy: tie stall barn, free stall barn, parlor, calf/heifer raising facilities; Beef: confinement, loose housing; Hog: confinement, farrowing house; Other)

Feed storage: (upright silos, bunker, harvestore, silo bags, grain bins, sealed high moisture corn unit)

Manure Storage: (pit, slurrystore, scrape and haul)

Machine Storage; other outbuildings

Type and condition of fences and tiling:

Septic system: (age & condition):

Water system: (age of well, recently inspected):

Electrical system: (stray voltage problems):

Any known environment hazards?:

(underground storage tanks, on farm dump, nonpoint source pollution – barnyard runoff, etc.):

How do you picture a transition taking place? What is the type of business arrangement you desire?

Sale Land Contract Share/Lease Cash Rent

Employee/Employer Lease with Option to Buy
(working agreement with future transfer)

Explain:

How long do you want or expect this transfer to take? Minimum (yrs/months) Maximum (yrs/months)

Comment:

What level of responsibility and management control do you wish to maintain during a transition of your farm business?

Explain:

Is your farm business, in its current state, generating enough income for an additional family? Yes No

If no, do you feel there are enterprises that can be added or expanded to generate additional income Yes No

Explain:

What are your expectations from a Farm Link match?

Identify your strengths, as a mentor and helper, to a beginning farmer that would contribute to a farm transition:

Comment on any "weaknesses" about yourself that may affect someone new working with you in this transition process:

Spouse Expectations and Comments - To be completed by spouse

How do *you* feel about your spouse's desire to transition the farm?

How do *you* expect to benefit from a Farm Link match? What do you see as your role in this transition process? Explain:

Conclusion of spouse questions. Feel free to add more information relevant to your interest in Farm Link.

REFERENCES – To be completed by Land Owner Applicant

Please list THREE references, *other than a relative*, at least one of which you have had a working relationship with - such as a former employer, co-worker, partner, etc.

NAME:	PHONE NUMBER OR ADDRESS	RELATIONSHIP
NAME:	PHONE NUMBER OR ADDRESS	RELATIONSHIP
NAME:	PHONE NUMBER OR ADDRESS	RELATIONSHIP

We occasionally get requests from the media to provide names of farmers who are interested in or have benefited from the Farm Link program. If you are willing to let us provide your name to the media (name only, no information which is confidential) please sign below.

I authorize the release of my name to the media for the purpose of being interviewed:

SIGNATURE OF LAND OWNER AND/OR SPOUSE	DATE
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Additional Information:

Any additional material or comments that would help a prospective farmer make a decision as to your potential qualifications for a Farm Link match is encouraged and may be included with this form.

Return to: WI Dept. of Agriculture, Trade & Consumer Protection
Wisconsin Farm Center
Farm Link Coordinator
PO Box 8911
Madison, WI 53708-8911



Wisconsin Department of Agriculture, Trade & Consumer Protection
 Division of Agricultural Development
 Farm Center
 2811 Agriculture Drive, PO Box 8911
 Madison WI 53708-8911



Farm Link - Prospective Farmer Application

This information form is to be completed by prospective participants in Farm Link.
 Please answer the following questions as completely as possible.

If you have any questions about completing this form, please call 1-800-942-2474

Case Number: _____

Farmer			
LAST NAME:	FIRST NAME	MIDDLE INITIAL	DATE OF BIRTH
ADDRESS:	CITY:	STATE:	ZIP:
HOME PHONE	WORK PHONE:	COUNTY:	# OF CHILDREN LIVING WITH YOU:
CURRENT OCCUPATION	DO YOU PLAN TO CONTINUE IN THIS OCCUPATION? <input type="checkbox"/> YES <input type="checkbox"/> NO		

Describe your educational background and your farm or other work experience:

Spouse/Partner			
LAST NAME:	FIRST NAME	MIDDLE INITIAL	DATE OF BIRTH
ADDRESS:	CITY:	STATE:	ZIP:
CURRENT OCCUPATION	DO YOU PLAN TO CONTINUE IN THIS OCCUPATION? <input type="checkbox"/> YES <input type="checkbox"/> NO		

Describe your educational background and your farm or other work experience:

Are you willing to relocate? Yes No If yes, please indicate areas:

Describe your housing needs: (style, size, age, condition, number of bedrooms, type of heat, number of baths):

What type of farming operation are you interested in:

Row crop Livestock Livestock & Row crop Other (please specify)

Livestock desired, check all those in which you are interested:			
	Number of head per year		Number of head per year
Dairy (No. milking)		Beef background	
Dairy young stock		Beef finishing	
Custom dairy heifers		Farrow-to-finish	
Cow-Calf		Hog finishing	
Other:		Sheep - birth to market	
Do you currently own livestock? <input type="checkbox"/> Yes <input type="checkbox"/> No			

If yes, list the livestock available for the farm transfer (indicate type and numbers, grade or registered):

Do you currently own machinery? Yes No

If yes, list the machinery available for the farm transfer (type and condition of major equipment) :

What is the total acreage you hope to work?

Total acres

Crop acres

Pasture acres

What type of farming practices do you plan to use?: (check all that apply):

Conventional tillage

No-till

Sustainable agriculture

Strip crop

Minimum tillage

Ridge-till

Organic farming

Rotational grazing

Comments:

Describe buildings and facilities that are desired, including size, capacity

Livestock facilities: (Dairy: tie stall barn, free stall barn, parlor, calf/heifer raising facilities; Beef: confinement, loose housing; Hog: confinement, farrowing house; Other)

Feed storage: (upright silos, bunker, harvestore, silo bags, grain bins, sealed high moisture corn unit)

Manure Storage: (pit, slurrystore, scrape and haul)

Machine Storage; other outbuildings

Type and condition of fences and tiling:

How do you picture a transition taking place? What is the type of business arrangement you desire?

- Sale Land Contract Share/Lease Cash Rent
 Employee/Employer (working agreement with future transfer) Lease with Option to Buy

Explain:

How long do you want or expect this transfer to take? Minimum (yrs/months) Maximum (yrs/months)

Comment:

Why have you chosen farming as a business?

Explain:

What are you willing to contribute to a Farm Link match? (Be specific where possible: include labor, capital, management, machinery, livestock, family assistance, spouse contribution, off- farm employment, etc.)

Explain:

Identify areas about yourself that you would like to improve:

What kind of additional training would help you in your farm operation? (computer, farm amnagement, mechanics, etc.)

Spouse Expectations and Comments - To be completed by spouse

Would you consider working within the farm operation? Yes No

Comments:

Were you raised on a farm? Yes No

Comments:

How would becoming part of a farming operation change your life-style and your family life?
How would you feel about making these changes? What would be the advantages and disadvantages to you and your spouse?:

Identify **your** areas of personal strength that would contribute to a farm transition:

Identify areas about yourself that **you** would like to improve:

Conclusion of spouse questions. Feel free to add more information relevant to your interest in Farm Link.

REFERENCES – To be completed by Farmer Applicant

Please list THREE references, *other than a relative*, at least one of which you have had a working relationship with - such as a former employer, co-worker, partner, etc.

NAME:	PHONE NUMBER OR ADDRESS	RELATIONSHIP
NAME:	PHONE NUMBER OR ADDRESS	RELATIONSHIP
NAME:	PHONE NUMBER OR ADDRESS	RELATIONSHIP

We occasionally get requests from the media to provide names of farmers who are interested in or have benefited from the Farm Link program. If you are willing to let us provide your name to the media (name only, no information which is confidential) please sign below.

I authorize the release of my name to the media for the purpose of being interviewed:

SIGNATURE OF FARMER APPLICANT AND/OR SPOUSE	DATE
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Additional Information:

Any additional material or comments that would help a prospective farmer make a decision as to your potential qualifications for a Farm Link match is encouraged and may be included with this form.

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