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Introduction

According to the 1997 Census of Agriculture, approximately 42 percent or 27,300 of Wisconsin's 65,600 farmers are age 55 or older. Given these numbers and current trends in the United States, approximately 22,000 Wisconsin farmers will retire during the next decade. There is little statistical information on how many of these farmers have developed an estate and retirement plan. Traditionally, in the farm community, the plan was simply to sell the farm to a son or daughter and move into town. Besides, farmers often say, they're too busy working to take the time to plan. Planning does take time, and often requires making tough choices. When faced with making tough choices, farmers, like the rest of the population, may choose not to make any decision at all. For the 22,000 potential farmer retirees of the coming decade, it's late, but not too late to start planning for retirement. For younger farmers who may be reading this guide, it's never too early to start.

Retirement planning for farmers is further complicated by the complex and rapid changes taking place in agriculture. Technological innovations, global competition in the marketplace, world economic and trade issues, changing government policies, urban pressures on agricultural lands, as well as conservation issues and environmental concerns all impact the choices and decisions facing retirees. This generation of farmers has already experienced dramatic times in American agriculture. Some of them lived through the Great Depression; most remember World War II and the post-war boom of the 1950s, 1960s, and 1970s. All of them dealt with the agricultural crisis of the 1980s. These life events have impacted not only this generation's financial health but the way they deal with financial and life decisions as well.

Because of the economic, social, environmental, and government issues that impact the decisions a farmer must make while planning for retirement, it is essential that farmers get good information to make the best decisions possible. Information provided in this guide is intended to give farmers an overview of the options and the opportunities available for retirement and estate planning. This guide is a supplement to *"Farm Transfers in Wisconsin, a Guide for Farmers."* It does not purport to have all the answers, nor is it intended to replace the attorneys, accountants, and other professionals farmers will need to work with, but it should provide some basic ideas on how to analyze, prepare for, and manage retirement and estate planning issues.

This guide was written by a variety of professionals in the retirement and estate-planning field including attorneys, accountants, and financial planners. It is intended to take the reader through the steps of retirement and estate planning in an easy-to-follow sequence.

Chapter 1

Retirement Planning

What do You Want to do When You retire?

What do you really want to do when you retire from farming? Chances are you have fantasies about the possibilities, things you have always wanted to do... travel, hobbies, visiting family and friends, just relaxing, trying a new career. The reality is that you may not know exactly what you want to do until you have the opportunity to try a few things. Perhaps you will find that there are several things you may want to try in your retirement. Check out all of the possibilities, keep your options open, and continue to dream!

Managing ones own business provides a high degree of freedom and flexibility, along with a tremendous amount of responsibility. When a farmer decides to turn the business over to a successor, he/she will most likely want to maintain that freedom and flexibility, plus some degree of responsibility.

Retirement is part of the growth process that spans a life-time. A great deal of thoughtful planning is necessary to make the change from active farming to a meaningful retirement that is full of opportunities and pleasant experiences.

Farming is a career that generates creativity. That creative energy will remain active as the farmer moves into retirement and an important part of the retirement planning process is to make sure there is ample opportunity for expression of that creative energy. Looking at retirement from this positive point of view is just as exciting as the dreaming a young farmer does as he anticipates starting his own farming operation!

As you begin to decide on what it is you want to do in retirement, a valuable tool to use is a goal setting exercise. You can begin with your own set of questions. For example: where do I want to live, what activities do I enjoy doing (list), how hard do I want to work, etc. Once you have listed a number of questions and listed your answers, prioritize your answers. Come back to the list periodically and revise it. Investigate or research some of the possibilities on the lists. Whenever possible, try one of the activities for a week or two to see if it feels as good as it sounds.

Discovering what you really want to do in retirement may take some time and effort, but that time and effort will pay great returns as you move into the retirement portion of the continuum of life.

There are many tools available to help you in making decisions about your lifestyle in retirement. The following Lifestyle Planning Survey may be helpful. Spouses should fill it out individually, and then compare answers.

Lifestyle Planning Survey

Life satisfaction is dependent upon both your physical well-being and your emotional well-being. Take the following survey to help you think through how you will spend time in retirement.

Physical Well-Being

What activities might you do to preserve your physical autonomy and self-sufficiency and to connect with others?

	Name:	Name:
Bowling		
Camping		
Dancing		
Fishing		
Gardening		
Golfing		
Jogging		
Skiing		
Stretching		
Tennis		
Walking		
____________		
____________		

Emotional Well-Being

What will you do to ***give back to others?***
Where might you ***volunteer?***

	Name:	Name:
Church		
Clubs		
Community		
Hospital		
Nursing Home		
Organizations		
Politics		
Senior citizens		
Sporting events		
Tutor/educate		
____________		
____________		
____________		

What will you do for ***personal growth?*** How will you get more out of life and develop courage to deal with life challenges? What will you do to gain greater wisdom?

	Name:	Name:
Arts		
Computer		
Cooking		
Crafts		
Financial		
History		
Language		
Mechanical skills		
Music		
Performing arts		
Personal skills		
Religion		
Sewing		
Technical skills		
____________		
____________		

What will you do to ***revitalize yourself?*** This includes those activities that will help you stay connected to daily life.

	Name:	Name:
Clubs		
Concerts		
Dining		
Employment		
Family		
Movies		
Museums		
Shopping		
Theater		
Travel		
____________		
____________		
____________		

What will you Need when you retire?

Where to live

This is the most fundamental place to begin. Often you have lived in the same house your entire life. It may have been your parents' or even your grandparents' home. Now that you are retiring, do you plan to move off the farm? If you stay on the farm, what will be your involvement in the farm operation? Will you be an active worker; a consultant; or a second-guesser? Remember, you built your vision. It's now up to the next generation to build theirs.

Are you a big fan of winter, or do you plan to move to a warmer climate? Will you have one primary residence or a winter and a summer residence?

Moving to a new location is quite a change. If you are considering this, begin scouting the new area out at least five years prior to relocating. Vacation there once a year, and get to know the neighbors and the neighborhood. It is a lot easier to move where you have friends, where shopping and entertainment are familiar, and where you have already established your health care network.

Financial Needs - Cost of Living

When you have a general sense of what you would like to do, you can work on your budget. Begin by identifying what you are spending today. Use the Monthly Family Income & Expenses worksheet that follows. Make the first column as accurate as you can. All of your retirement cash flow needs are based on it. This is a great exercise to do as a couple to help you determine what you value today, and are likely to value in retirement. If you don't know how much you spend on food, entertainment, clothing, incidentals, car care, utilities, and other monthly costs, keep track of every penny you spend for the next several months; then divide to determine monthly estimates.

When you have the base for your expenses, add in dollars for hobbies and activities. Don't make decisions about what you can and cannot do until you actually work out the numbers.   You will be amazed how much you can do, as long as you understand what is important to you.

Examine each interest in more depth. Do you have everything you need to begin (or expand) those interests? If not, you must determine what it will cost initially and what will it cost on an annual basis to enjoy it. Do this for each activity.

Remember to add in some money for new vehicles. Whether you plan to finance them or pay cash, make sure you have budgeted for their replacement. Expect to replace a vehicle every 3-5 years, assuming you will keep two vehicles.

Remember that you are planning a budget that will last you 20 to 40 years.

Things that will disappear

Once you retire, there are many expenses that will go down or disappear completely. For most the biggest change is debt repayment. Whether you are selling your farm, or letting the next generation take over the operation (and the debt), this will affect both your cash flow and your tax flow. Factor this effect into both areas.

The same is true of all other farm-related expenses. Look only at personal expenses, unless you plan to run a small farming operation for your mental and emotional well being. Plan for a full and active retirement.

The next area to look into is taxes. This includes state and federal income taxes, as well as Social Security taxes. A good portion of your income should be non-taxable. You may be able to have $50-$70,000 of taxable income, and still be in a 15% federal income tax bracket. On the other hand, you will be losing many of your deductions, once you have sold off your farm assets. For that reason, you need professional guidance on when to sell, what to sell and how to sell.

Your only savings need will likely be for future vehicles and vacations.

When you factor in the elimination of the seasonal financial uncertainty farmers feel when working, financial stress can be a thing of the past.

Take the time to complete the following cash flow worksheet.

MONTHLY FAMILY INCOME & EXPENSES

Client Name | Date:

	CURRENT	ANTICIPATED RETIREMENT
INCOME		
Client #1 (# Paychecks/yr.__________)		
Wages / Salary		
Bonus		
Social Security		
Pension / IRA		
Client #2 (# Paychecks/yr.__________)		
Wages / Salary		
Bonus		
Social Security		
Pension / IRA		
Taxable Interest		
Tax-Exempt Interest		
Dividends		
Rental Income		
Other (ex: Alimony, Child Support, etc.)		
Other (ex: annuity pymts, etc.)		
TOTAL	0	0
EXPENSES - OTHER		
Income Taxes / Withhheld or Estimated		
Client #1		
Federal Tax (filing status: _______________)		
State Tax (filing status: _____________)		
Social Security + Medicare		
Client #2		
Federal Tax (filing status: _______________)		
State Tax (filing status: _____________)		
Social Security + Medicare		
Estimated Taxes - Federal		
Estimated Taxes - State		
TOTAL TAXES	0	0
Savings and Investments:		
Pension / 401k / TSA (Client #1)		
Pension / 401k / TSA (Client #2)		
Car Fund		
Vacation Fund		
Other Systematic Savings / Invt.Club, etc.		
IRA Contributions (Client #1)		
IRA Contributions (Client #2)		
Roth IRA Contributions (Client #1)		
Roth IRA Contributions (Client #2)		
UTMAs / Contrib.for Children's Education		
Variable Universal Life-add.to Cash Value		
TOTAL - SAVINGS & INVT.	0	0
EXPENSES - COMMITTED		
Basic Housing Expenses:		
Real Estate Taxes		
Mortgage Payments (P+I)		
Home Equity / 2nd Mortgage		
Home-Owners / Renters Insurance		
Rent		
Gas / Oil / LP + Electric		
Electric		
Water / Sewer / Garbage		
Telephone		
Maintenance & Repairs		
Yard & Lawn Care / Cleaning Service		
Miscellaneous Household		
TOTAL - BASIC HOUSING	0	0

	CURRENT	ANTICIPATED RETIREMENT
Food / Clothing / Transportation		
Food / Groceries / Cleaning Supplies		
Clothing / Laundry / Dry-Cleaning		
Auto Loan / Lease Payments		
Auto Insurance		
Gas and Oil		
Auto Maintenance & Repairs / License		
Public Transportation / Parking		
TOTAL-FOOD/CLOTHES/TRANS.	0	0
Other Committed Expenses:		
Doctor / Dentist (Out-of-Pocket Expenses)		
Prescription Drugs / Medical Supplies		
Education-Adult / Child / Etc.		
Personal Care / Hair / Non-Prescrip.Drugs		
Dependent Care / Day Care		
Alimony / Child Support Payments		
Legal / Finl.Advisor / Accountant		
Dues		
Misc. Committed Expenses		
Life Insurance (cost of insur.) - 1st client		
Life Insurance (cost of insur.) - 2nd client		
Disability / Long-Term Care - 1st client		
Disability / Long-Term Care - 2nd client		
Medical Insur. (note whether pre/post tax)		
Other Insurance (Umbrella, etc.)		
School Loans / Business Loans		
Personal / Installment Loans (non-auto)		
Tax Payment for Prior Year		
Credit Cards / Charge Accounts		
Other Obligations		
TOTAL - OTHER	0	0
TOTAL - COMMITTED EXP.	0	0
EXPENSES - DISCRETIONARY		
Charitable Contributions		
Dining Out		
Fun (movies, concerts, sports events, etc.)		
Recreation / Vacation / Travel		
Hobbies / Sports / Camp		
Gifts (Birthdays / Holidays / etc.)		
Home Furnishings / Decorating		
Newspapers / Magazines / Books		
Cigarettes / Cigars / Liquor		
Kids' Sports / Lessons (music, soccer, etc.)		
Veterinary / Pets		
Cable Television		
Spending Money / Allowance		
Other Discretionary / Misc.Purchases		
TOTAL - DISCRETIONARY	0	0
TOTAL - (Comm.+Discret.+Svgs.)	0	0
SUMMARY:		
TOTAL ANNUAL INCOME	0	0
TOTAL ANNUAL EXPENSES	0	0
NET DISCRETIONARY INCOME	0	0

Health Care Issues

There is one major area of risk to your financial security in retirement that we have not addressed, health care costs. Even the best-drawn plans can be cast into disarray by the onset of major health problems. Besides the personal toll, major illnesses can damage your financial well being and literally compromise the quality of care a person can afford. Here again, you need professional advice.

Medicare

Medicare is a federal health insurance program for 1) people aged 65 or older, 2) people of any age with permanent kidney failure, and 3) certain disabled people under age 65. The two parts of Medicare are (Part A) Hospital Insurance, and (Part B) Medical Insurance. The medical insurance pays for doctors' services and other related medical services.

There is a seven-month window to enroll during Medicare's "Initial Enrollment Period". This window is the three months before you turn 65, the month you turn 65, and the three months after you turn 65. When you apply for Social Security, your application for Medicare is automatically included. Also, when you enroll in Part A of Medicare, Part B is automatically included, unless you say you do not want it.

As you are probably aware, there are some health care costs that Medicare does not fully cover or does not cover at all. There are five basic ways to fill these gaps.

1. Pay these bills "out-of-pocket".
2. Purchase Medicare supplemental insurance, often called Medigap coverage.
3. Enroll in a managed care plan that has a Medicare contract.
4. Continue coverage under an employer-provided health insurance program, if you are eligible for such protection.
5. Qualify for either full Medicaid benefits or some state assistance in paying your Medicare costs.

Medicaid

Medicaid is a joint federal and state program that covers medical bills for the needy. If you qualify, it will pay your long-term health care costs. Unfortunately, Medicaid is welfare. In order to qualify, you'll have to spend down your assets, leaving your spouse impoverished, and potentially risking your farm assets. While Medicaid is a program available to everyone, it should only be your choice of last resort.

Long Term Care Coverage

There are varying degrees of health care in the long-term care continuum. When planning for your long-term care needs, the possibility of needing any one of these types of care should be taken into account.

Custodial Care

This consists primarily of attention to personal needs, often referred to as activities of daily living, or "ADLs". Custodial care includes help with transportation, bathing, eating, and administering regular medications. Personnel without professional medical skills can often perform this type of care.

Intermediate Care

Intermediate care is occasional nursing care that must be performed by or under the direct supervision of skilled medical personnel. This type of care is not as intensive as full-time skilled nursing care.

Skilled Nursing Care

This is the most intensive type of care and is normally associated with an extended stay in a nursing home. It is also associated with short-term care (convalescent care) required for acute conditions such as a broken hip or recovery from a heart attack. Skilled care can only be performed by or under the direct supervision of skilled medical personnel.

Funding Options

There are four ways to deal with the costs of a long-term care need. They are:

1. Self-Insure using your accumulated assets to cover the need. This can be difficult if transitioning the farm to the next generation.
2. Look for family assistance to provide care or to cover costs.
3. Protect against the potential need with a comprehensive Long-Term Care insurance policy. Here you must weigh the policy costs against the asset risks of self-insuring.
4. Spend your assets down to qualify for Medicaid.

Legal Issue

It is critical that certain precautions are taken to ensure your health needs are met with a minimum of inconvenience and a maximum of dignity. Documents such as Health Care Powers of Attorney and Living Wills are examples of legal precautions you can take. These are dealt with in greater detail in Chapter 6.

Life Expectancy

The final concept to discuss is 'Life Expectancy'. Life expectancies are quoted in articles and in the media, but few people truly understand what they are.

Example *A couple today, both age 65, have a joint life expectancy of 22.0 years. Compare that to their individual life expectancies of 18.2 years (hers) and 15.0 years (his). Let's simplify this by just focusing on one of the retirees, the wife.*

At age 65, the wife has a 'life expectancy' of 18.2 years. What this means is that, according to past studies, if there were 1,000 women age 65 today, in exactly 18.2 years, 500 of them will have died. These numbers were set with historical data from the 1950's, 1960's and 1970's. People are now living longer than they were back then, and that trend does not appear to be slowing down. At the 18.2-year life expectancy, half of the women are still alive at age 83. That is how life expectancy is measured.

Mrs. Farmer is now a part of the 500 women who survived to age 83.2. This group has a new life expectancy of 8.3 years. In other words, 25% of the original 1,000 women are expected to still be around and active at age 91.5. For those keeping score, this 25% now have a life expectancy of an additional 5 years. See the problem? Life expectancies are tossed out as if everyone is expected to die within a few months of their 'life expectancy'. That is not how these statistics work. There is greater than a 50% chance you will exceed your current life expectancy.

So what should you do?

Look at your current health status. How is your health compared with others of your age? Don't compare yourself to a younger version of yourself 10 years ago. Remember that even if you have a serious condition, you may still have a long future in front of you – so it is best to be realistic on the positive side.

Consider you family health and longevity history. Keep in mind that that just because a condition is common to your family, you personally may not be at risk because of changes you have made in your lifestyle.

Evaluate your current lifestyle. Assess both beneficial and harmful behaviors, especially those related to a healthy heart. The lifestyle habits most associated with heart disease are overeating, high fat foods, low-fiber diets, smoking and sedentary lifestyles.

When in doubt, plan to age 100. It is safer to have money left over when you die, than to plan to 'Die Broke'. Small changes in your rate of return can have a marked impact on your investment portfolio. Play it safe! Assume you will be around for a long time. The more active you are, the more likely this is to be true. Let 'life expectancies' remain what they are, interesting statistical data, but plan for a full life.

The Five Basic Areas That Affect Your Retirement Financial Planning.

- Your Lifestyle and Your Legacy
- The Financial Environment
- Converting Assets to Income
- Human Problems That Can Derail You
- Your Financial Philosophies

Your Lifestyle and Your Legacy

The monies and assets you have accumulated throughout your working life will go to one of two purposes, your lifestyle or your legacy. It's up to you to decide how much is dedicated to each purpose. You are in control. But where to start?

The first determination you need to make is how much of your asset base is needed for your lifestyle needs. This is where those computer models can help. Use a lower rate of return, a higher expense need and a moderate inflation assumption in order to plan conservatively. Be conservative in your approach, but also be realistic. Build in goals you are sincerely interested in pursuing. If travel is of interest, add it in. If a condominium on a golf course in Arizona feels out of place, leave it out. This is your lifestyle plan. Add in everything you have an interest in. Only leave things out that you truly do not care about. You are designing a strong, safe foundation for your retirement dreams, not a *how little do I need* scenario. Once you have done this, you will know what you need to provide for your retirement.

Of course, even with conservative assumptions, something could happen down the road that you did not foresee. As with any business plan, you need some safeguards. Protect yourself by taking the financial figure you calculated above and add on another 25, 30, 40 or even 50%. This should take into account most market swings.

Finally, keep a separate cash reserve equal to a couple of years of income needs in addition to that base. Now you are prepared for almost any catastrophe.

Example: *Let's say that you need $50,000/year for your retirement lifestyle. Taking into account all of your guaranteed sources of income (such as Social Security and pensions), your computer model says you need a retirement nest egg of $400,000. You decide to add on another 30% ($120,000) for safety. Then you add a cash reserve of $100,000 (two years' income needs) for protection against market volatility. Your total fund is $620,000 ($400,000+$120,000+$100,000).*

It is vital you feel safe and secure with your retirement income. That makes this an area where professional assistance is crucial. An objective third party can verify that you have thought through all of the possible contingencies. That person should understand your vision and your philosophy, but also challenge your thinking.

Your objective here is to remove all financial stress from your retirement years. Once you have accomplished this, you can begin to plan your legacy. It is important to think about your legacy in conjunction with lifestyle planning because your legacy already exists. You do not have to wait for death in order to share it.

Your legacy, in the simplest of terms, is the dollars and assets that you have accumulated that will <u>not</u> be spent on you. Since these are dollars you will not spend, someone else will. That is what makes it your legacy. You get to make the choice as who ultimately benefits from your labors.

Controlling Your Legacy:
Your legacy can go in any of three directions: to the government, to your heirs, or to charities. How much goes to each is your choice within some limitations.

So what are the steps you need to take? Now that you know the size of your potential legacy, you must decide where you want your legacy to go. Start by considering these questions..

- *What do you want your heirs to get? The farm? The farm debt?*
- *What about the non-farm heirs? What is fair for them?*
- *What is the most important thing you can leave to your kids? Is it your work ethic? Your money?*
- *Will the inheritance make them better off? Leave them without the need to achieve?*
- *What outcomes do you want your legacy to produce?*
- *What values do you want your legacy to influence?*
- *When do you want to share your legacy? Now? At death?*

There are no universal truths to follow when dealing with these questions. There also is no set formula to determine what is fair. But what you choose to do with your assets will have a dramatic impact on your heirs.

The disposition of assets will have a different impact on heirs taking over the farm than they will for the non-farm heirs. Farm heirs need the farm assets if they are to run the business. A $1,000,000 farm operation will still need to be worked long and hard to keep it profitable. The $1,000,000 farm is less likely to be seen as a financial windfall by the farm heir than the $500,000 check to a non-farm heir. The non-farm heir may see it differently, though.

When the farm itself is not the issue (meaning no one wants to take over the farm operation), you need to decide whether you prefer to give assets, income or both.

There are many strategies you can employ to create income streams for your heirs, rather than giving them large sums at once. The choices are yours.

The Financial Environment

While you can control your lifestyle and your legacy, you cannot control the next area we will deal with, the financial environment. The financial environment is the world we live in. Or perhaps, a better description of the financial environment is that it is the rules that define the world we live in. While you cannot control the rules, you need to know them in order to play the game. These rules include such things as tax laws, interest rates, the stock market and inflation.

Someone once said taxes and inflation do not destroy wealth, they simply move it from those that do not know the rules to those who do. The lesson here is: Learn the rules.

Tax laws

Tax laws are complicated, but they are theoretically designed to ensure that everyone pays their fair share of taxes.

Tax rules are very complex. You may not be getting all of the breaks you are entitled to. If you do not understand the rules, they can work against you. You can correct this either by learning all of the rules, or by putting together your own team of knowledgeable advisors.

Interest Rates and the Stock Market

Interest rates and the stock market represent the return on your investments. This is the financial environment most of us think of. The assumptions you make in regards to investment performance have a dramatic impact on your income streams, and on your needed nest egg. While you cannot absolutely control investment returns, you can direct their performance by how you invest.

If you sell your farm, how will you invest the proceeds? Will you use land contracts as a part of your retirement strategy? If so, how will you set a fair rate in terms of interest and number of years? Will it be enough for your retirement needs?

Will you invest in stocks, bonds, mutual funds, annuities, or CDs?

What is your targeted return? 6-8%? 8-10%? 10-12%? Are you basing your expectations on market performance of the last 5 years, last 10 years, last 20 years or last 70 years? Take a long-term view when it comes to investing. Be safe and prudent.

Inflation

It is critical to build an inflation assumption into your retirement projections. We know expenses will increase over time. Will your income? Either your income increases over time, or your lifestyle decreases.

Example*: Assume you have $500,000 invested to yield 8%. If you have an income need of $35,000/year, the income of $40,000 ($500,000 @ 8%) is more than adequate. After 5 years, assuming a 3% inflation rate, your annual needs have gone from $35,000 up to $40,575. After only five years of retirement, you are now facing an annual shortage. Inflation can be a silent killer.*

You can prepare for inflation in a few ways. You can set up income streams that fluctuate along with specific markets. You can keep some financial investments growing at a more aggressive rate (say 10-12%), while using up the principal and interest on more conservatively invested assets. Let me show you what I mean.

Take that same $500,000 we talked about. If we invested $250,000 of it at 6%, and the remaining $250,000 to return 10%, we still have an 8% average yield. In the case above, we *took the gains off of the entire amount, producing $40,000 of fully taxable income. Instead now, we will take $35,000 of principal and interest out of the $250,000 earning 6%. (You would invest for stability of principal here with moderate income.) That would last us almost 10 years. By investing the other $250,000 at 10% for those 10 years, it has grown to $650,000. (At 12% it grows to over $750,000.) Now you have the ability to increase your income.*

Inflation strategies need to be built in since certain expenses cannot be eliminated. Property taxes and medical expenses are not optional. Entertainment is. Without an inflation strategy, your retirement years will not be the reward you deserve.

So how do you prepare for all of these financial environmental issues? Deal with what you can control. You control your assets and your income sources.

Converting Assets to Income

Let's analyze your retirement income sources. They fall into four categories: Farm income sources, Personal (Non-Farm) income sources, company pensions and Government benefits.

Farm Income Sources:

Your farm is likely to be your largest asset when you reach retirement. While this is not always the case, it is the case with smaller farms. An important point for younger farmers to consider is the more non-farm assets you can accumulate for retirement, the greater your flexibility in transitioning your family farm. Farm assets consist of land, buildings, livestock and equipment. The challenge is to convert substantial farm assets into an income stream. You can do this through a number of strategies. In broad terms, your options include 1) selling; 2) leasing. Consider the following choices as they impact your retirement cash flow.

Sale of Assets

A Lump Sum sale or cash sale is the easiest sale to deal with. When you sell an asset for a lump sum, you exchange your assets for investable cash. You are no longer responsible for that asset, nor for the income it produces. Your responsibility is to invest your cash to get a reasonable cash flow for your retirement lifestyle needs. You must pay any attributable income taxes.

Installment sale strategies consist of a cash flow that is made up of three components: principal, gain and interest. These provide a higher cash flow to the recipient than an interest only strategy, but with a longer-term risk. Here is an example.

Assume that you sold some farm assets valued at $123,000, with a $23,000 cost basis. After paying $23,000 in taxes in capital gains, you now have $100,000 to invest. If you invest your $100,000 at 8%, you would get an interest income stream of $8,000 (100% taxable) each year. At a 35% income tax bracket, you keep $5,200.

That same $123,000 (before taxes) set up for a 20 year installment sale at 8% would pay $12,528 each year. That is a 56+% increase in cash flow. The installment sale income stream is *also partially non-taxable. This income stream consists of some principal (your basis), some capital gain (the appreciation) and some ordinary income (the interest). Because of taxes, you would not keep all $12,528, but using the same tax assumptions as above, you would keep about $9,146. Almost $4,000 more. Of course after 20 years, you would have no principal left. That is the trade-off you face.*

Land contracts are a popular installment sale technique because they allow the current owner to 1) establish a guaranteed income stream; 2) spread taxes out over a number of years; and 3) help out the next generation in buying the farm. It is the last point that often leads to a Land Contract decision. If your heirs do not qualify for credit, you may choose to become the bank. You may also decide that you can extend a more favorable loan rate than prevailing market rates. A Land Contract effectively removes all future asset appreciation from the seller's estate, yet the farm assets still secure the payments.

The potential drawbacks of a Land Contract fall into four primary areas.

- First, your income stream has an expiration date. It is your responsibility to invest the surplus funds to provide for your lifestyle needs after the Land Contract has expired.
- Second, your income stream is a set dollar amount, providing you with no protection against inflation. Again, it is your responsibility to invest the surplus cash flow to cover future inflated retirement needs. This is a critical concern if you have set an extremely low interest rate on the Land Contract.
- Third, your retirement fortunes are still tied to the profitability of the farm operation. You have not eliminated your financial stress. This risk may manifest itself in the way you attempt to *manage* the farm after retirement. After all, if you have $500,000 tied up in a Land Contract, do you have the right to express your thoughts? This better be agreed upon at the time you sign the Land Contract.
- Finally, the remaining balance of the Land Contract will be included in the estate at the death of the seller.

Self-Cancelling Installment Notes are an alternative to Land Contracts where the remainder of the debt is forgiven at the death of the seller. This provides estate tax protection, but no residual for the non-farm heirs. Other attributes are similar to Land Contracts.

Private Annuities are another approach that can be used. Unlike a Land Contract, a Private Annuity has an indefinite ending date. By design, a Private Annuity will continue to pay an income stream to the seller as long as he/she is alive. As with Self-Cancelling Installment notes, the debt is forgiven at death, removing the asset as well as the appreciation from the estate.

To the seller, there is the assurance that he/she cannot outlive the income. The buyer, on the other hand, benefits from an early death, but bears the risk of longevity of the seller. While the seller acts as the bank with a Land Contract, the buyer acts as a pension company with a Private Annuity.

The other disadvantage to the buyer is that interest payments are not tax-deductible.

Leases

Equipment leases are a simple way to convert assets to direct income. The owner and the leasee agree on basic lease terms such as which equipment, what time frame, and the annual lease payments. At the end of the lease, everything is back to how it started. With a Lease With An Option To Buy, you would also agree to a final buy-out figure. Now the equipment ends up changing hands at the end of the lease. Another often-used strategy is a straight lease with the salvage value of the equipment being gifted to the lessee (normally an heir) at the end of the term.

Land leases are a very common way to produce additional retirement income. Here the retiring farmer maintains ownership of the land and leases its use out. Payment can be a preset cash figure or crop shares.

Land leases are used for a few reasons. Often, when transferring the farm to the next generation, you want to allow that next generation time to build up equity. Saddling them with a large debt on land, or installment payments, may keep them from being profitable. A land lease keeps their expenses down. Conversely, future appreciation on the land remains an asset of the property owner.

By setting up the lease payment as shares, the retired owned has the capacity to share in increased profits to help offset inflation. There is downside risk also, dependent on commodity prices.

Alternatively, by adjusting your cash lease annually, you can set your lease terms according to farm profits from the previous year. Here you run the risk of charging low prices in an up year and high prices in a down year.

To a large degree, competitive pressures will determine your lease price. If land is at a premium, so will lease prices be. If land leases are plentiful, prices will decline.

Gifting

Direct gifts to heirs do not improve your cash flow, but they can be an important retirement strategy when selling off your farm assets.

When we discussed Land Contracts versus Private Annuities, one factor we did not discuss is the difference in the gifting options available for each. The owner should take all Land Contract payments and invest the surplus as a protection for inflation and longevity. With Private Annuities, longevity is not an issue. Payments are guaranteed to the owner as long as he/she is living. This allows the owner to make gifts to the purchaser, presumably a family member, during the early years of the transition, when cash flow will be the tightest.

With equipment leases, it is common for low-valued equipment to be gifted at the expiration of the lease. The owner received a good cash flow, and the equipment ends up with the ultimate user.

Charitable Gifting can be an attractive option when you have substantial taxes to pay in a sale, or when you prefer to pass income on to your heirs, instead of assets**.** Gifts to a charity or a charitable remainder trust reduce your taxable estate not only by the value of the gift, but also its future appreciation.

If you retain the right to the income from the asset, as in a charitable remainder trust, the estate tax savings will not be as large. However, you may choose to keep the income for your lifestyle, or make gifts of the income each year to children, grandchildren or a trust on their behalf. Note: If a portion of the income from the charitable trust is given to an irrevocable trust (or adult children) which purchases life insurance on the life of the donor, you will be able to transfer a substantial amount of money to your heirs which is not subject to either income tax or estate tax.

A taxpayer can contribute an asset (usually highly appreciated and low income producing) to a charitable trust and receive a current income tax deduction. The trust can sell the asset and pay <u>no</u> income tax (capital gain or ordinary income), and then reinvest the entire proceeds at a higher rate of return. The trust will normally pay out a higher return than the donor previously received. This, coupled with the income tax deduction, can create a substantial increase in cash flow. A portion of this income can then be used to purchase a life insurance policy with the heirs as beneficiaries.

Example: *You are a 70 year old retired farm couple with 500 acres, valued at $2,000/acre, or $1,000,000 total. You are leasing the land at $100/acre, or $50,000 annually. Real estate taxes cost you $15,000, so you net $35,000.*

You are reluctant to sell since you may lose $200,000 to taxes. You place the land into a Charitable Trust that sells the land (with no tax impact) and reinvests the proceeds. At a 6% payout, you get $60,000/year, instead of $35,000. You also get a substantial tax write-off (Perhaps $400,000 or more) for your gift. You could then replace the $1,000,000 to your heirs with insurance and an Asset Replacement Trust on an income and estate tax free basis.

(Put the ASSET REPLACEMENT TRUST DIAGRAM Here)

Personal (non-farm) Income Sources:

IRAs or Qualified Pensions are the first non-farm income source you will probably look at. The reason for this is quite simple. The government will help you fund these plans.

In a high income tax year, maximize your available pensions. A Simple IRA allows you to shelter $6,000 ($12,000 if you both claim farm income) or 100% of your income, whichever is less. There are other plans that allow you to go considerably higher. The key is to take advantage of this tax break.. Choosing the proper pension plan should be done in consultation with your financial advisor and your tax consultant.

In years when farm income is low, you should consider taking advantage of the Roth IRA. Your investment is non-deductible, but the dollars grow tax-deferred, and can be withdrawn tax-free in retirement. A couple, both age 35, could invest $4,000 each year through age 65. If they made 10%, they would have $650,000. At 12% it would grow to almost $1,000,000. (Even at 4% inflation, that $1,000,000 is worth almost $250,000 today.) Roth IRAs are not deductible, but in a low tax year, that is not a critical benefit. (In the above example, remember that $1,000,000 would be tax-free.)

Company pensions can offer tremendous advantages to farm families. If your spouse works off the farm, her company may be putting dollars aside for your retirement lifestyle. Many firms offer 401(k) s with a company match. Always take advantage of that match. Do not underestimate the value of job benefits. Health and pension benefits take tremendous pressure off of farm families.
Government Benefits: Social Security is a system of social insurance benefits available to all covered workers in the United States.   Begun in 1937, the Social Security system covers a wide range of social programs. The term "Social Security", as it is commonly used, refers to the benefits provided under one part of the system, OASDI. (This acronym actually means Old-Age, Survivors and Disability Insurance.)

OASDI benefits are funded primarily by payroll taxes paid by covered employees, employers, and self-employed individuals. Both the OASDI portion of the payroll tax, as well as that part of the tax that goes to finance hospital insurance, HI (Medicare), are provided for under the Federal Insurance Contributions Act, FICA.

While benefits are based your earnings, there is an optional formula you can use to gain a year of credit in years you have a loss. For farm families, the disability segment of OASDI may be the only long-term disability you can get. In addition, the retirement income and Medicare benefit provide a great deal of security in your retirement. This is a very low cost program, considering the benefits you are entitled to receive.

Human Problems That Can Derail You

What happens at death?

Everyone will die sometime. It is a fact of life. The only question is when. When one spouse dies, there is emotional and economic change for the survivor.

Adjustment Costs

Emotionally, there is a great loss at the death of a spouse. People grieve differently. One woman built a garage and put up a yard fence within a year of her husband's death. It was something they had talked about, but never got around to doing. A cost like this needs to be built into a survivor's plans.

Travel Costs

Some people need more family companionship to cope with the change. Going to visit kids or bringing them in more often is quite common. A contingency fund to cover travel should be considered.

Health Insurance Costs

If you have a personal health insurance policy, the cost will go down if there is only one person to be insured. If the coverage came from the spouse's employer and the spouse died, your costs will go up when getting a personal policy. This needs to be factored in.

Tax Costs

Taxes will change in two ways. Some income would disappear (such as the deceased spouse's Social Security) dropping the taxable income down, but the filing status will also change, raising your tax brackets.

Daily Living Costs

Daily living expenses are the other areas you should look into. There will be some savings when there is only one person, but costs do not drop in half. You may go to one vehicle rather than two, but real estate taxes remain the same. Look at each expense separately.

Benefits that change

Benefit changes can affect you two ways. Income benefits may disappear, and new benefit expenses may appear. Examples of potential disappearing benefits include Social Security, Health insurance, Life only pensions, and Estate Tax breaks. New benefit expenses are primarily health insurance related.

Who will do what spouse used to do?

Additionally, you may incur new expenses from activities your spouse used to do. Examples are basic house repairs, dining out (versus cooking), yard care, and numerous other daily tasks. Are these tasks you will assume, or will you have to hire help?

What happens in case of a Long-Term Care need?

According to the AARP (American Association of Retired Persons), long term care is the single largest out-of-pocket health care expense we face in retirement. The U.S. Government Accounting office projects that by the year 2018, the U.S. nursing home population will grow by 76%.

Medicare is limited in what it covers in long-term care costs, and Medicaid requires a major forfeiture of assets to qualify. For farm producers, the risk is greater than the population at large. This is because most of your retirement income is from asset income, rather than pensions. Should one of you have a long-term care need, most of your assets are vulnerable.

Costs that Change

Expenses will change similar to the death scenario discussed above. There is no reduction in income to the family, but there is the cost of the long-term care need. This could range from a few thousand dollars a year to thousands of dollars a month.

Income Sources

Long-term care expenses can be covered from five sources. Here is a quick overview of what each provides.

- Medicare – Full coverage the first 20 days, partial the next 80 days, nothing thereafter
- Current Income – At home spouse can keep a set (by the state each year) monthly income, with all surplus being attachable
- Current Assets – At home spouse can keep a set (by the state each year) amount, with all surplus being attachable
- Long Term Care policy – Private coverage to protect your assets and your income
- Medicaid – Full coverage, once you (and your spouse) are destitute

Risks to the at-home spouse

Long-term care costs are your responsibility as long as you have income and/or assets. Once these are gone, the state (through Medicaid) takes over.

The protection to an at-home spouse includes a limited amount of financial assets, and a monthly income. While these limits change annually, in round numbers, the at-home spouse can keep under $2,000/month of income and under $100,000 of financial assets. This creates a large hardship for a family when most of their income is from farm sources. It also puts the farm itself at risk. If mom or dad enters a nursing home, farm assets can be attached. In most cases, this can be prevented with good long-term care insurance protection.

Your Financial Philosophies

We touched on your philosophies briefly in the section dealing with your legacy, but we need to talk about them in more depth. Your philosophies must be aligned before your visions can be.

I had to work for it. So should they.

Depending on how you got your farm (or went to college; or paid for your marriage; or…), your views on transitioning the farm could be quite different. It doesn't matter what your parents did, or how the neighbors structured theirs. What matters is what you want to do. Before you discuss this with your kids, the two of you need to discuss it. Do not talk to the kids until you both agree.

I don't really need to live too fancy in retirement.

Farming has traditionally paid in assets, rather than in income. Therefore, for most of your lives, you have felt financially strapped. It is hard to change your stripes in retirement, and you do not have to. On the other hand, why did you sacrifice all of those years? Is there a payback you are entitled to? This is a very difficult issue for many farm families. It is the classic lifestyle versus legacy decision.

I do not believe in insurance.

Be open-minded when you look at which tools may work for you. For many of the things you want to accomplish, insurance will be the only vehicle that works well. Insurance can help you equalize your estate for the non-farm heirs. Insurance can keep the next generation from being saddled with overwhelming debt. Insurance can replace assets gifted into charitable trusts. Insurance can offset estate shrinkage, and protect your assets from the ravages of a long-term care need. Insurance can be used to move money out of your "C" corporation to you on a tax-free basis.

The stock market is too risky for retired people.

The real risk in retirement is not keeping up with inflation. As long as you prepare your portfolio to weather the ups and downs of the market, you should be safe. Growth stocks are a long-term proposition. They should be used for your legacy dollars, and for income needs that are a number of years away (at least 5 years). Other stocks (such as Utility stocks and Blue Chip stocks) pay high dividends and are therefore appropriate for current income needs.
The key is appropriate balance, and keeping a watchful eye on your assets.

Why worry about retirement? I won't live too many years.

The fastest growing segment of the population is people over the age of 100. Plan to reach the century mark. If you are wrong, you will have a greater legacy. If you are right, you will be prepared.

Getting my taxable income to zero every year saves me the most money.

There is a prevalent view in many farm operations that getting to $0 taxable is the best thing to do. This prevents you from qualifying for personal disability income insurance policies. It also prevents you from funding larger pensions. Social Security also becomes more limited in its scope.

Use all of your deductions each year, but before you decide to create new tax write-offs in December, decide how much income you should be willing to pay 15% on. Calculate your retirement using a minimum Social Security benefit, and then again with a higher benefit plus a pension. See how much you actually save with those December tax breaks. Your financial advisor and tax consultant should be able to help you quantify the impact of each tax decision.

Planning is only for the wealthy.

Actually planning is for everyone concerned about the future The key is the value you derive from planning. Would you be better off by planning your future? Would you be better off knowing the rules? The choice is yours.

Planning is too time consuming.

For many people, time is spent doing one of two things, work or stuff. Work is feeding the livestock, milking the cows, planting the fields, and all of the other tasks involved in operating the farm. Everything else is *stuff*.

Michael Gerber in "The E Myth" calls it ***working in*** the business versus ***working on*** the business. When you work on the business, you take the time to check your bearings to make sure you are headed in the right direction. When you work in the business, you make sure you are moving as quickly as you can in the direction you are heading (right or wrong). . When you work on the business, you take charge and run the business. When you spend all of your time working in the business, the business runs you. You need to spend some time doing both. Make sure your work schedule has some planning time built into it.

Chapter 2
Family Issues and the Survival of the Farm

When looking at retirement and estate planning most individuals are aware of the financial, legal and business management issues that need to be addressed. These concerns can be addressed by using financial planning worksheets, looking at the legal impact of various transfer methods and developing clear, realistic plans to achieve your goals.

Of equal significance in making the best possible decisions for retirement, transfer of the family farm and estate planning present another group of factors. These factors overlay the more familiar ones listed above and deserve equal consideration in the decision making process. They involve family and emotional considerations which are often more difficult to identify, understand, or explain than the factual information typically found in financial spreadsheets, legal documents and business plans.

Decisions made during retirement and estate planning have a significant impact on the quality of life during retirement. Failing to take into account family and emotional factors can undermine the best laid retirement and estate planning. Factors which should be considered include:

- Look at family history, including the expectations of those family members involved in the farm operation and those not involved. Family history should be examined in a forthright and open manner to help prevent hard feelings within the rest of the family.

- Consider issues of fairness versus equality when dealing with different members of the family. This is especially true under the following circumstances: a) some younger generation family members are involved in the family farm and others are not b) where there will be an unequal distribution of an estate for other reasons.

- Decide whether you are willing and able to make decisions which maximize the opportunity for family members to take over your farm operation.

- Recognize the inherent conflict between these two competing needs: a) the older generation's need for involvement and oversight; b) the younger generation's need for trust and autonomy in the management of the family farm.

- Acknowledge the tension between the older generation's desire for privacy and the benefits of openness and sharing between the generations when retirement or estate planning decisions are being made.

Ignoring these factors may have disastrous consequences for even the most carefully designed retirement and estate plans.

Identifying Potential Pitfalls

Gathering information to help you identify potential family concerns should be a part of your retirement and estate planning. Consideration of these factors, before moving forward with your retirement or estate planning will help you when you are making difficult choices. Some of the questions you will want to ask includes:

- Are there family members, besides you and your spouse, who are a part of the farm operation and will be directly impacted by your decisions?

- Do non-farm family members have a clear picture of the contributions made by and compensation paid to those family members involved in the farm business over the years?

- Do family members involved in the farm operation have an expectation that they have "earned" an interest in the farm business operation through their participation in the business? If so how will they be compensated?
  *gifts
  *equity transfers
  *partnership interest
  *share in a family corporation
  *equity building assets (i.e., breeding stock).

- Is there an expectation on the part of anyone in the family, that they or another family member will receive a larger share of the family farm?

- Is it more important to you that your estate be divided equally between your children? Is it more important that your farm business be transferred to the next generation?

- Is it important to other family members that your farm remain a part of their family history?

- Are there family members not currently involved in the farm operation who may want to become involved when you retire?
  *If so, can the farming operation financially support this?

- If the estate is to be divided equally, with an option to purchase the farm business for one of the family members, will the purchase of the family farm by one of the beneficiaries create a high-risk, financially unstable operation with inadequate capitalization?

- If the estate is to be divided unequally so that the farm business can be distributed to one or more family members how might this affect other family members?

- If selling the farm real or personal property outside the family is the only way to fund retirement, how will this affect other family members who want to see the farm kept in the family?

- If the farm will be sold, will it be sold as farm land or sold for development either to a land developer or to individuals?
  *Is there a way to sell part of the farm and retain part?

Are you planning on retiring completely from the farm operation or do you want to remain a part of the farm operation during your retirement? How will this impact family members who are a part of the farm operation?

Keeping Family Informed

One of the most important tools in getting the information necessary to make decisions and helping other family members understand and accept your decisions is open and honest communication. Keeping family members informed about your plans and letting them know why you are making certain decisions may head off problems down the road. Meeting with family members to discuss the impact your retirement will have on the farm operation can help establish a basis for understanding and acceptance. Meetings can be accomplished through individual conversations with children, meetings with family members involved in the family business, and meetings with the whole family and/or extended family members are all options.

Involving your children is important even if none of them are directly involved in the farm operation. A family meeting can give you the opportunity to provide information, clarify decisions and get input from family members to develop the best possible options for meeting your retirement needs and fulfilling your estate plans.

If your farm operation includes other family members one of your first priorities will probably be keeping them informed about the impact your retirement and estate planning will have on their own families. This will reduce the stress and potential conflict that would be likely to result if they know that you are planning for your retirement but don't know how that will impact them.

An awareness of the importance of understanding the impact of your decisions on your family and your farm operation before moving forward with your retirement and estate planning will help you make the best decisions both for you and your family. The involvement of other family members in the process can be very helpful in allowing you to get the information needed to make the best decisions. In addition, family members who understand the process used to determine how your assets will be distributed, may have an easier time accepting the final decision, especially if there is an equal distribution or an unequal distribution which recognizes contributions made to the family business may have an easier time accepting the final decision.

The timing for a family meeting will vary with each situation, however, if other members of the family are involved in the farm operation it is especially important to keep them informed and make them a part of the planning as early as possible. When meeting with family it is important to establish some ground rules to make communication as helpful as possible for the participants. Some things to remember in planning family meetings include:

- Meetings should be held at a time and in a place that will allow the participants to maintain a businesslike environment.

- An agenda may help meetings flow better and may help keep participants focused on the issues at hand.

- Everyone should have an opportunity to talk and ask questions. Meetings should provide parties with an opportunity to share their expectations and concerns. Family members should be given the chance to express emotional issues and work them through with other family members.

- Respect should be shown to other family members even if you disagree with them. Sometimes options that seem unworkable or impractical contain elements of wisdom that can make the final decision a better one.

- All family members should be encouraged to participate fully in the discussions and decision making process. People tend to support and be committed to decisions they were involved in and understand.

Distributing Your Assets

There are many difficult issues that must be dealt with during the retirement and estate planning process. Perhaps the most difficult of these is deciding on a pattern of distribution for your estate. For farm families this decision is harder than for those families whose estate planning does not involve a family business operation. A farm is not just an asset, but represents an entire lifetime encompassing both business and personal aspects of family history. Because of this the decision regarding what to do with the family farm is important to each farm and non-farm family member. Often this decision making process will involve consideration of whether or not fair and equal mean the same thing. Making this decision is not a quick or short process when there is more than one child in the family.

First, defining the terms “equal”, “unequal”, and “fair” is important. An equal division is fairly easy to explain and understand. It involves placing a value on all assets, both real and personal property, and dividing those assets equally between all family members. In an equal distribution each family member receives the same amount of property. This may mean that each individual receives an equal share of each asset; however, that may not necessarily be the case. For example, when dividing up personal property one family member may get the family china and another the family silver. If one of these is worth more than the other, the individual receiving the less valuable item would receive other property to equalize the two distributions.   When an estate is distributed equally, each family member should end up with property of equal value.

Treating all family members equally is of course the easiest and most straightforward way to distribute an estate.

An unequal distribution of assets occurs when one family member receives property of a greater value than the property received by another family member. If one family member receives real estate valued at $100,000 and another family member receives personal property valued at $25,000 the estate would involve an unequal distribution of assets.

Fairness involves an individual's judgment regarding distributions made by an estate plan. What is fair? Is equal fair? Is unequal fair? Fairness is determined by how each individual feels about their treatment, whether it be equal or unequal, in an estate plan. Although the predominant belief is that "fair" and "equal" are the same, there are many reasons why an unequal distribution may be fair in estate planning. There may be younger children who need continued support from their parents' estate while their adult siblings can be expected to support themselves. Financial circumstances have allowed parents to provide better education or other opportunities for one child and they want to somehow "make it up" to a less fortunate child. One child may have special needs that must be addressed. In some cases, one child may have provided support which allowed a parent to remain at home rather than in an assisted living situation and the parent may want to reward that child's efforts. And of particular importance in planning for the transfer of a family business, if one or more children have been actively involved in making a family business successful the parents may want to take these contributions into account during estate planning. Although there is no easy definition of what is "fair" in estate planning, each of these situations contain a common thread. They require reflection on the question of whether or not equal or unequal distributions are "fair" given other circumstances.

Example for Chapters 2 and 3:

Father and mother have farmed for fifty years. Initially they farmed with father's parents, however, for the last thirty-five years they have operated the farm first alone and then with their oldest son and his wife. Their oldest son quit his job working as a diesel mechanic and returned to the farm ten years ago because his father had been diagnosed with cancer.

Father and mother know that if their son and his wife had not returned to the farm they would probably not have been able to continue farming because of father's surgery and treatments for cancer. They also know that although their son is paid for his work on the farm his income is significantly less than he would have made had he continued as a diesel mechanic. They were somewhat surprised when their son decided to leave his job and come home to work on the farm because he was doing quite well in his job and they were not able to give him the same income or benefits. Having their son on the farm has also helped considerably with equipment repair costs because he has been able to keep equipment in top notch condition, keeping their repair bills down and enhancing the resale value of the equipment. In addition to the help their son has given them with the *farm, he and his family have also helped out in other ways. Their grandchildren have helped them by mowing their lawn, helping with heavy cleaning jobs and shoveling in the winter. Their daughter-in-law has driven them to doctor appointments, helped get their farm records set up on their computer, and helped out in other ways especially when either of them have been ill.*

When their son came home ten years ago, they had planned to do something about setting up a partnership or family corporation so they could pay him with a share of the farm ownership in addition to his wages. Unfortunately they never followed through with this plan and now they are concerned with the position this leaves their son with regard to his ability to take over the farm.

Father and mother are now planning to retire from the farm. Although father's cancer has not returned, he never got back the energy he felt before his chemotherapy and has not been able to "carry his load" in his mind. In addition, father has experienced some new health problems that make it desirable for him to slow down. Father and mother need retirement income and also want to plan for how their "Century farm" will be passed down to the next generation.

Father and mother have two other children, a son and a daughter. They have a fairly good relationship with all three of their children, however, they know that their younger son feels that his older brother is taking advantage of them. He knows his older brother gets paid for working on the farm, plus he gets a house and other benefits. He has also made comments about the fact that his brother's children have been given animals to show at the fair and that they "get money all the time from Grandma and Grandpa". When the family gets together he has made references to the fact that he thinks his brother's family gets "everything". His sister has told mother that he has told her he is worried about whether or not there will be anything left for his parents to retire on. His sister thinks that his real concern is how much will be left over for him. His sister also thinks that part of her brother's frustration comes from the fact that he assumes that his parents made it "worth it" for his brother to leave the good job he had to go home. Sister has no idea how much her parents are paying her older brother but she has seen how much her older brother's family does for their parents in addition to the farm work. She believes that without the help her parents get from her brother's wife and kids they wouldn't have been able to maintain their home on the farm. She also has seen how much enjoyment her parents get from their relationship with their grandchildren. As far as she is concerned she would rather see her parents happy and comfortable in their own home than worry about money. Although there have been no arguments, everyone in the family agrees that there is an increase in tension whenever all the kids get together, mostly because of younger brother's feelings.

Father and mother have never shared any financial information about their assets or farm business with their younger son or their daughter, including the amount of pay and other compensation given to their older son. They gave each of their children the opportunity to come home and work on the farm. Since neither their younger son and his wife or their daughter wanted to leave their jobs and friends and move back home they figured that the business arrangements between them and their older son were no one else's business.

Their older son realizes now that he should have done more planning before he came home. He had the impression that father and mother were planning to make him a partner in the farm, however, that has not happened. His low wages and uncertain future have caused problems between himself and his wife. Although his wife knows how much he wants to stay on the farm she believes that they do not have the resources to buy the farm from his father and mother either when they retire or from their estate when they have passed away. She gets along well with his parents but in the last few years has been frustrated because she feels that they are never going to have anything of their own. She knows that given their current financial picture, the farm real and personal property are worth far more than they can afford to pay. She is worried about their future now that her husband's parents are planning to retire.

In this scenario, father and mother will have to make some difficult choices. They will have to decide whether their goal is to allow their son to continue farming or whether their goal is to maximize the assets available to finance their retirement by selling the farm business. They will also have to decide between a retirement and estate plan which provides for equal treatment for all of their children and fair treatment for their oldest son who has made it possible for them to continue farming for the past ten years.

Assume that father and mother have not determined how they want to divide their estate between their children, but they have established some goals for their retirement and estate plan. The three major goals that they want to accomplish with their retirement and estate planning include:

1) They want sufficient retirement income.

2) They want their farm to remain in the family if at all possible.

3) They want each of their children to feel positive about how they are treated in their estate plan.

Is there a way for father and mother to accomplish all of their goals? Is there a way to provide them with an adequate retirement income without burdening their oldest son with excessive debt? Will an estate plan which provides equally for all their children be fair given their older son's involvement in the family farm business?

At this point father and mother will have started considering a number of options. As father and mother are beginning to make decisions they will probably want to include other family members in the planning process. Communication can help ease the tension and stress created by lack of knowledge which is likely being felt by all family members especially other members who are directly involved in the farm operation. It is probably in everyone's best interest to hold a family meeting. This will provide other family members with knowledge that each might need to make decisions regarding their future. In the example outlined above, this is especially important for the older son and his wife who will be directly impacted by any decision made by father and mother.

Father and mother and their older son and his wife may have had regular farm meetings in the past to discuss business decisions but if they have not, it is important that they begin to meet to discuss plans being made by father and mother. This will allow their son and his wife to begin to make plans for their own future. Where multiple generations are involved in a farm operation, it is clear that there will be changes for everyone involved in the farm operation whether the farm stays in the family or not. Although father and mother may have a fairly clear idea of their options, including son and daughter-in-law in the planning can help them make sure that they have explored all available options.

Father and mother may also want to include their other children in the family meetings. This will give father and mother an opportunity to let their other children know what their goals are and help them understand how their decisions are being made. It is likely that their children are probably aware of some of their parents' goals, however, by including their children in the planning, father and mother can help them understand their decisions. Letting everyone know why decisions are being made is especially important if their plans for retirement or estate plans involve a sale or other transfer of assets to their older son or if there is to be an unequal division of assets within the parents' estate plan. Keeping everyone informed, including those family members not part of the family business, will help diffuse bad feelings, jealousy and suspicions that one family member may be taking advantage of another.

The first and most obvious option they looked at involved selling all of the farm assets. This would free the assets up for their retirement and would make it easier to divide the proceeds in their estate equally between their children. If they take this option, father and mother would like to give their oldest son the opportunity to purchase the farm from them. They have discussed whether or not selling the farm to their son at a reduced price would be fair to their other children. They are also uncertain whether their son would have sufficient assets to obtain a loan for the purchase of the farm and realize that they may have to consider other options such as selling the farm on a land contract.

Another option they are considering would result in their keeping the farm at this point. Under this option they would rent the farm to their son or farm with their son on shares thereby keeping the farm and farm personal property intact. This option might impact *their retirement since it might result in their continuing to be involved in the farm operation. In their estate plan, they could transfer the farm to their oldest son and distribute other assets to other family members. Whether or not this would result in an equal distribution would depend on the amount of resources available. If there are not sufficient assets to distribute the farm to one family member with equal distributions to other family members, issues of fairness will need to be addressed.*

As you can see, making decisions regarding the fate of a family farm business is a very complex process; one which requires information, communication and thoughtful decision-making by the farm owners. The process is not an easy one; however, it can be a very rewarding one when family members are involved and can understand and accept the decisions that are being made.

Chapter 3
What Happens to the Family Farm?

What happens to the family farm? Making this decision requires careful consideration of a wide range of options available to the older generation. Retiring farmers generally have farm real estate as well as farm and non-farm personal property. They may also have other assets such as non-farm real estate, life insurance, retirement accounts, cash or other investments.

Of course, the easiest way to deal with retirement and estate planning is to sell off assets to fund retirement and set up an estate plan in which the estate is divided equally among all beneficiaries. There are many options available for maximizing the available equity in farm assets.

The farmer could continue to operate the farm as long as he or she is physically able. Continuing to operate the farm business will not allow the retiring farmer as much flexibility during retirement, especially if the farm operation includes livestock. Transfer of the farm would occur when the farm owner dies. Although this will allow the farm owner to continue to make management decisions about the farm operation, it also requires more careful planning for disability and distribution at time of death.

A major concern as the farmer ages is whether or not he or she will be able to continue making decisions until death. Illness, injury or age related disabilities may limit the farm owner's ability to make appropriate management decisions. It is important that a plan be put in place to deal with decision making in the event of disability of the farm owner.

Even if the farm owner chooses to continue operating the farm until he or she dies, the farm business could be transferred into a corporation, limited liability partnership or general partnership. Family members could be given a share in a corporation or partnership by gift or as compensation for any services they rendered on behalf of the farm business.

Establishing this type of business structure could also provide for an orderly transition of management in the event of disability. In addition, resources could be transferred to the younger generation by providing compensation in the form of a percentage of the profits at the end of the year or a share of farm products (i.e. a heifer calf or a percentage of the crops) based on the younger generation's ownership interest in the family farm operation.

It is important that the farm owner consider how the farm is to be treated at the time of death. Options for transfer when a farm passes through an estate are much more limited than those that are available during the farm owner's life. The opportunity for a gradual transfer of the farm business by gift or transfer of ownership interest as a part of employment compensation ceases with the death of the owner. Retaining ownership through death makes it more important that the farm owner put in place an estate plan that will carry out his or her desires.

There are other options available that can provide more flexibility in retirement and free up assets for retirement income. First, the retiring farmer could begin the transfer process for the farm by bringing a younger farmer into the operation. This could be a family member interested in eventually taking over the farm or it could be an unrelated individual that the farmer has chosen to take over some of the daily work and management of the farm operation.

This option requires a commitment on the part of the retiring farmer as well as on the part of the younger individual. Both parties need to clearly define their roles both now and for the future. If the goal is to transfer the farm to the younger individual, a plan for transferring the farm business should be discussed and put in place. Obviously this situation will work best if both parties share similar goals and objectives for the future of the farm operation.

To determine whether or not the interests of the farm owner and younger individual are compatible, there are many issues that should be addressed. It is important to set goals and develop a plan to accomplish this type of transfer. Some important factors to consider include:

- Are both the retiring farmer and the younger generation farmer committed to making sacrifices necessary to make the transfer of the farm successful?

- Does the retiring farmer or the younger generation farmer have sufficient assets to successfully fund the transfer?

- Are the financial and management goals established realistic given the personalities, family responsibilities and needs of both the retiring farmer and the younger generation farmer?

- Does the current farm operation provide sufficient cash flow to fund the financial and management goals of both the retiring and the younger generation farmers? If not are there changes in the operation or accommodations that can be made to allow the transfer to be financially successful?

- Are there other family members who have concerns, issues and emotional feelings that may have an impact on the success or failure of the transfer of the farm?

- Will family members accept a plan that over time results in a shift of the family farm to another individual or group? Will acceptance be affected by whether or not the transferee is a family member or a non-related individual? If there is difficulty with acceptance on the part of other family members, will the lack of acceptance undermine the transfer?

Once a decision has been made to transfer the family farm, there are many options available to begin the process during retirement planning. The older generation could establish a business structure for the farm such as an S corporation, a limited liability partnership or a general partnership that could distribute shares in the corporation or a partnership interest to the younger generation farmers as compensation for the labor on the farm. This option can provide the younger individual with an opportunity to build equity and/or an ownership interest in the farm business.

An estate plan could provide an option for the younger generation members of the farm operation to purchase the farm business, either at market value or at a percentage of fair market value, if they have sufficient assets. This allows the farm owner to put in place a plan which would recognize the younger individual's contribution to the farm business while still providing non-farm family members with a share of the estate. Where the younger individual is a family member who is involved in the farm operation and the estate has other assets sufficient to finance retirement and accomplish other estate planning goals, the farm could be transferred to the family members involved in the farm operation with the non-farm heirs receiving cash or other assets from the estate.

Another option would establish an estate plan that gives one or more family members the farm business, even though this involves distributing a larger share of the estate to them. This could be done to allow the farm business to be transferred to those members of the family who have been involved in the operation.

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Another possibility would be for the retiring farmer to downsize the farm operation or to discontinue the farm operation completely. In this situation, the first course of action would likely be to decide how the farm operation is to be disposed of. The farm owner could decide to sell off unnecessary personal property. This would free up assets currently tied up in livestock and machinery which are no longer needed because of the change in the farm operation. Unnecessary real property could also be disposed of by selling cropland and retaining the residence, any adjoining buildings, and a smaller amount of land.

The farm owner could sell the farm real property to a younger farmer, either a family member or a non-related individual, who would continue to operate the farm. If the purchaser intends to continue the current farm operation the sale might also include the sale of farm personal property.

If there is no one who is interested in or able to continue the farm operation, the farm might be sold for commercial or residential development. The farm owner could either sell the entire farm to a developer or could develop the land for residential or other purposes on their own.

If the farm were sold, estate planning would be much simpler. The proceeds from the sale could be invested in other assets. At the time the estate is settled all assets could be appraised to establish the total fair market value at the time of death. When the estate is distributed, each beneficiary would receive an equal share of the assets in the estate.

There are, of course, many variations of these options available for disposing of the farm business. Deciding which is the best plan for you and your family is a very personal choice and will depend on circumstances within your family and farm operation.

Chapter 4

Defining Your Financial Estate

What is an "Estate"?

Your estate includes all property interests that you own or have an interest in. This includes assets owned outright by you, as well as interests you may have in a trust. Liabilities, including mortgages, notes and accounts payable that you owe a third party, reduce the net value of your estate. It is extremely important to determine exactly what you own and how it is held when you are making estate planning decisions. Many types of property have a document of title. Examples include a deed for real estate, car title, stock certificate and savings bonds. The document of title will help you determine what your interest in the property is. Ownership of assets that do not have a title is usually established by physical possession.

Determining what assets are in your estate and establishing ownership is important for a number of reasons. It is important to know what your interest in property is because you cannot transfer assets to others if you do not own them or if another individual has a right of survivorship.

It is also important not to omit assets from your asset inventory. This is especially important when you are estimating the value of your estate for tax purposes since property that an individual owns at death is included in his or her estate for estate tax purposes at the fair market value on the date of death (or the fair market value six months from the date of death if the alternate valuation date is elected). To determine the value of your estate you will also need to establish your ownership interest in assets.

There are different terms that refer to specific types of estates. Examples include a probate estate, guardianship estate, and a trust estate. Each of these “estates” have two things in common: a) the estate is created by law or a legal document and b) an agent appointed by law or designated under the terms of the legal document creating the estate manages the assets for the benefit of the individual ward/s or beneficiary/ies of the estate.

What is a "Probate Estate"?

All of your assets that do not pass by operation of law or by contract pass through probate. This would include any property that you own individually, that is titled solely in your name, or in which you have an undivided interest. Some examples would include property such as real estate, stocks, cars, boats, personal effects, etc. Probate refers to the court proceeding required to transfer the assets of a decedent that do not pass directly by law or contract. Your probate estate consists of those assets that must be transferred through a court probate proceeding.

What is a "Trust Estate"?

A trust estate is made up of assets which have been transferred to the trustee of the trust. The trustee manages these assets for the benefit of the beneficiaries designated in the trust document. It is important to remember that simply creating a trust does not transfer assets into the trust.

What is a "Guardianship Estate"?

If you are determined to be incapable of managing your properly a guardian may be appointed by the court to manage it for you. If a guardian is appointed to manage your "estate" he or she will take control of any assets you still own. Careful estate planning can help you avoid the necessity for appointing a guardian of your estate. If you have a trust and or a Power of Attorney that designates someone to manage your affairs in the event that you become incapable of doing so, the appointment of a guardian for your estate may not be necessary.

How is property owned?

Property can be owned in a number of ways. The type of ownership interest will determine whether the ownership of the property transfers automatically when the owner dies or whether the ownership interest must be transferred another way, for example through the use of a will or trust.

Property interests which are held by one person are solely owned or individual property. The owner of such property has the right to sell, give, bequeath or otherwise convey his or her solely or individually owned property. It is important to remember that title alone does not establish ownership interests between married couples. Under Wisconsin law a spouse may have a marital property interest even if their name does not appear on the title or deed. Other types of restrictions imposed by law, such as zoning, public right of way, prohibitions against acts of nuisance, and other similar restrictions, also limit the sole or individual owner's complete control over property held in his or her name.

Property interests held by more than one individual can be held in several ways including as joint tenants, tenants in common, marital property or survivorship marital property. Each form of ownership has different characteristics and will impact estate planning differently.

Joint tenants each have an interest in the entire property during the period of the joint tenancy. At the time of death the interest held by one joint owner goes directly to the surviving joint tenant/s regardless of the terms of the owner's will. Joint tenancy property does not become a part of a probate estate but passes by operation of law to the survivor.

Tenants in common each have an undivided interest in the whole property during the period of the tenancy in common. An undivided interest means that none of the tenants own a particular part of the property. Each tenant owns the property in common with the other tenants. There is no right of survivorship. During the lifetime of each tenant, he or she may sell their interest or transfer it by gift. After the death of each tenant, the property passes under the terms of a will or trust or by the laws governing intestate succession. Each owner can transfer only their share of the property. Property held as tenants in common becomes a part of the owner's probate estate.

Marital property is property owned by married persons. In Wisconsin all property owned by spouses is presumed to be marital property in which each spouse has an undivided one-half interest. At the time of death, each spouse has the right to transfer his or her interest in marital property as if it were his or her solely owned property. There are exceptions to the marital property presumption. This includes property owned before January 1, 1986, retirement plans owned by the surviving spouse, and property acquired by gift or inheritance, some personal injury payments, etc. The exceptions are outlined specifically in Wis. Stat. 766. It is best to discuss concerns with an experienced estate planning attorney.

Survivorship marital property is marital property which transfers automatically to the surviving spouse upon the death of his or her spouse. Holding property as survivorship marital property can provide a very beneficial tax advantage to the surviving spouse. Upon the death of the first spouse, the surviving spouse gets a stepped up basis on all survivorship marital property. For example, assume that the spouses purchased a farm for $50,000 thirty years ago. The farm is now worth $320,000. After accounting for improvements made and depreciation taken, the current basis in the farm is $80,000. Sale of the farm would generate a capital gain of $240,000. Unless the farm is held as survivorship marital property, only the decedent's half is given a stepped up basis, meaning the survivor would be liable to tax on one-half of the gain, or $120,000. If the farm is held as survivorship marital property, there would be no capital gains tax due at the sale price of $320,000, the current fair market value.

What categories of property are included in your estate?

Your estate is made up of real property and personal property. Each of these has certain characteristics that place the property into one of these categories.

Real Property: Real property is land, anything growing on the land, and anything that is permanently erected on or attached to the land. *Examples*: Land, fences, barns, silos, personal residence, trees, and mineral deposits under the land (unless these have been transferred to another party).

Personal Property: There are two types of personal property.
Tangible personal property is an asset that can be felt or touched. Certain improvements to land that can be removed from the land or buildings are considered personal property. In some cases, ownership of tangible property is established by a document of title. For many types of tangible property ownership follows the physical possession of the asset. *Examples of types of tangible personal property are*: *Automobiles, livestock, machinery, stored grain, tools, and furniture.*

Intangible Personal Property is generally represented by a written document that has no value itself but which serves to identify the asset and show how the asset is owned. *Examples are* *checking accounts, savings accounts, certificates of deposit, stocks, bonds, retirement accounts, brand or trade names, goodwill, patents, copyrights, money market funds and promissory notes.*

Life insurance is another type of intangible property. Life insurance is slightly different than other types of property because while it may have no value or a much smaller cash value during your lifetime upon your death the face value is due. For example, term life insurance has no cash value during your lifetime but the face value of the policy becomes an asset of your estate when you die. Other types of policies, such as whole life, universal life and variable life insurance, have both an insurance value and a cash surplus or cash reserve that has value during your lifetime.

How are the assets in my estate distributed when I die?

By Operation of Law: Some forms of property ownership determine, by legal definition, who will get the property at the time of the owners' death. *Examples* include joint tenancy, survivorship marital property and payable on death (POD) accounts.

By Contract: You can arrange to have property transferred to designated beneficiaries upon your death under various contracts including life insurance, retirement plans and annuities. Ownership passes to the designated beneficiary at the moment of your death. Distribution of proceeds from insurance policies, retirement plans, U.S. Savings Bonds, P.O.D. accounts or other assets with a designated beneficiary can be disposed of by will only if the deceased person named his or her estate as the beneficiary.

By will: A will is used to distribute property according to the wishes of the person making the will, called the testator. A will can transfer only assets in which the testator has an ownership interest that survives his or her death. Assets passing by operation of law or according to contract cannot be transferred by will. A will is a written document that specifies the who, the when, and the how of the transfer of your property at the time of your death. A will can also include other important provisions such as the naming of your personal representative and nomination of a guardian for your minor children.

By Trust: A trust can also be used to control the transfer of your property at death. A trust is a legal device that allows you to transfer property to a trustee. A trustee will manage the property, as directed by the trust, for the benefit of the persons you designate. The trustee can be the individual creating the trust, a family member, trusted friend, or neutral third party such as a bank trust company. Assets held in trust at the time of death are not subject to probate. There are two types of trusts,

By Intestacy: Assets owned by a person who dies without a will are transferred by the laws of intestacy. All states including Wisconsin have laws of intestacy that say how property is distributed. Property under intestacy law passes to relatives of the decedent. An individual who dies without a will is said to have died intestate

Record Keeping

Attached is a worksheet to help you keep track of all of your assets, liabilities and other important information. Updating this worksheet annually will make a dramatic difference in helping others settle your affairs if you become incapacitated or if you die. In addition, documents that are difficult or impossible to replace should be stored where the danger of destruction is minimal. For example, important documents should be stored in a safe deposit box or a fireproof safe.

Examples of how an estate is transferred at death:

Martial Property: Effective January 1, 1986 Wisconsin enacted the marital property law. the marital property law presumes that all property of spouses is marital property. Each spouse owns one-half of all marital property. At the death of the first spouse, one-half of the marital property is included in the spouse's estate and is distributed pursuant to his or her will (or other estate planning documents) or the Wisconsin intestacy laws.

Joint Tenancies with Right of Survivorship: Each of the two or more owners has an equal, undivided interest in the whole asset. A decedent's share automatically goes to the surviving joint tenant(s) at death. Nothing the estate planning documents say make any difference as to who gets the property. (An example of this is payable on death (POD) accounts.). In Wisconsin spouses may also create survivorship marital property that is similar to joint tenancies.

Tenant in Common: Unlike a joint tenancy, if property is held as tenant in common there is no survivorship provision and the decedent's interest in the property is transferred as if it were solely owned property.

Qualified Retirement Plan Benefits and Individual Retirement Accounts: These assets go directly to the beneficiary as you specify bypassing probate.

Life Insurance Proceeds: The policy payoff is part of your contract with the insurance company and it goes promptly to whomever you direct with no probate.

CONFIDENTIAL
ESTATE AND RETIREMENT PLANNING QUESTIONNAIRE

DATE: ________________

I. Personal Information:

Husband's Name: ____

Birthdate: ____________________ Social Security Number: ___________________________

Wife's Full Name: ____

Birthdate: ____________________ Social Security Number: ___________________________

Date and county/state of your marriage ___________________________________

Home Address: ____

Home Telephone: ( ) ____

E-Mail Address: ____

Business Address:

Husband ____

Wife ____

E-Mail Address: ____

Business Telephone: Husband ( ) ____________________ Wife ( ) ____________________

Seasonal Residence: ____

Seasonal Telephone: ( ) ____________________

II. Personal Advisors

Attorney: ____

Address: ____

Telephone: ( ) ____________________

Insurance Agent: ____

Address: ____

Telephone: ( ) ____________________

Stockbroker ____

Address: ____

Telephone: ( ) ____________________

III. All Children: (If any children are adopted or of a previous marriage please indicate)

Name	Birth-Date	Soc. Sec. Number	Address, City & State

IV. Married Children:

Child	Spouse's Name	Grandchildren Names	Grchild. Birthday

V. General Family Information:

Does any child or grandchild have a health problem or handicap?

Yes ___ No __

If yes, please explain:

____

____

Are there any other persons dependent upon you? Yes ___ No __

Monthly obligation: Alimony $ ________ for ___ years

VI. Current Estate Plans:

Does Husband have a will/trust at the present time? Yes ___ No __

Location of original(s): ____

Does wife have a will/trust at the present time? Yes ___ No __

Location of original(s): ____

Do you have a marital property agreement? Yes ___ No __

VII. Real Estate (Personal Residence, Second Residence and Rental Properties):

Location	Ownership*	Basis	Estimated Cost	Value	Mortgage Balance

*See explanation of ownership by Wisconsin married persons at end of questionnaire.

VIII. Bank Accounts and Certificates of Deposits:

Type of Institution	Account	Ownership*	Approximate Balance

IX. Stocks and Mutual Funds: (Indicate if subject to margin account)

Company	No. of Shares	Ownership*	Cost	Approximate Mkt. Value

X. Bonds (Taxable and Exempt), Treasury Instruments, Notes and Accounts Receivable:

Description	Due Date	Face Value	Market Value	Ownership

* See explanation of ownership by Wisconsin married persons at end of questionnaire.

XI. Life Insurance

Please furnish the requested information for all policies on members of your family, including husband, wife and children. Be sure to include group insurance through work. Please use additional sheets, if necessary.

In lieu of completing this portion of the questionnaire, you may be able to obtain computer printouts from your insurance agent.

Ins. Co.	______	______	______	______
Policy #	______	______	______	______
Insured	______	______	______	______
Owner*	______	______	______	______
Type Ins.	______	______	______	______
Face Val.	______	______	______	______
Cash Sur. Val.	______	______	______	______
Annual Prem.	______	______	______	______
Loans	______	______	______	______
Primary Benef.	______	______	______	______
Conting. Benef.	______	______	______	______

XII. Retirement Plans:

If either spouse is entitled to any benefits under a deferred compensation, retirement or profit sharing plan, please furnish the following information:

Participant	______	______	______	______
Plan Name	______	______	______	______
Plan Nature	______	______	______	______
Expected Payment	______	______	______	______
Death Benefit	______	______	______	______

* See explanation of ownership by Wisconsin married persons at end of questionnaire.

Contribution Made By Whom	____________	____________	____________	____________
Designated Benef.	____________	____________	____________	____________
Life Ins. in Plan	____________	____________	____________	____________

If either spouse has established an IRA account, please furnish the following information:

Contributor	____________	____________	____________	____________
Investment	____________	____________	____________	____________
Approx. Value	____________	____________	____________	____________
Designated Benef.	____________	____________	____________	____________

XIII. Interest in Trusts or Estates:

Does any member of your family have any relationship to an existing trust as donor, trustee or beneficiary. Yes ___ No __

Has any member of your family in the past received an inheritance from an estate? Yes ___ No __

If so, please explain:

____

____

____

____

____

____

Does any member of your family have any interest (e.g. as a beneficiary) in any pending estate? Yes ___ No __

If so, please explain:

____

____

____

____

____

XIV. Personal Effects:

Please list all items having significant market value, such as jewelry, art, antiques, rare musical instruments, autos, boats, collections, etc. Please Note: Normal household furnishing need not be listed.

Description	Ownership*	Est. Value

*See explanation of ownership by Wisconsin married persons at end of questionnaire.

XV. Closely Held Business Interests:

Company name ____

Existing Benefits: ___ Group Life ___ Group Health

___ Medical Reimbursement ___ Disability ___ Split Dollar

___ Qualified Plan ___ Deferred Compensation

XVI. Other Assets:

If either spouse has any other assets of significant value which are not listed above, please give details.

____

____

____

____

____

____

XVII. Liabilities (Other than real estate mortgage):

Creditor	Amount Due	Date Payable

XVIII. Gifting:

1. Have you or your spouse made any gifts in any one year to any person which exceeded in value either:

   a. $10,000, if made by you alone, or
   b. $20,000, if made by you and your spouse?

   Yes __ No __ If yes, specify the amount of gift, date and donee ___________

   ____

   ____

   ____

*Ownership of Property by Wisconsin Married Persons

Wisconsin's Marital Property Law has changed the legal concept of ownership. As between married persons, ownership is no longer governed solely by how title to an asset is held. Under marital property the determination of the ownership of an asset depends on whether an asset was acquired or is traceable to an asset acquired before the marriage, as a gift or inheritance, from a trust, or from income or earnings after the marriage. While title to an asset no longer determines its ownership, title does govern who has the right to manage and control the asset with respect to third persons.

Under the ownership column, you should provide first how title to asset is held (such as husband only (H), wife only (W), husband and wife (H&W)) and second, if the asset was acquired or can be traced to an asset acquired before the marriage (Prior to Marriage), as a gift or inheritance (Gift or Inheritance) from a trust created by a third party (Trust), such fact should be noted.

Chapter 5
Building Your Estate with Non-Farm Assets

Back 100 years ago, it would not have been unusual to find a farm raising cattle, hogs, chickens and maybe even a few geese. Add in some corn, some tobacco and a few other cash crops, and what you had was a diversified farm venture. This diversification provided financial security by preventing a farm from being hit too hard from one poor commodity market. It also limited what the farm had to sell in the marketplace.

As time passed, farm producers learned that by specializing in specific areas, they could better focus their talents, thereby increasing profitability. New farms became dairy farms, or hog farms, or cranberry farms. The loss of diversification was offset by increased specialization due to knowledge, experience, and technology. Still, most farms today rely on the market prices of only one or two commodities. It can often be feast or famine.

We all learn from the past, but the strategies you use to build your farm's profitability will not work in building your non-farm assets. You need to take a similar, but more comprehensive approach.

First, learn from your grandparents. You need to diversify assets. There is security in balance. Next, approach the market the way your parents did, with specialized knowledge. Do not simply scatter money or chase returns. Know what you are investing in and why. These are the keys to building financial assets.

Why should you build financial assets?

Security

The old saying warns 'not to put all of your eggs in one basket'.
Your first priority is to create greater safety and security for your family. As you know, farm markets are quite volatile. You have learned to offset this volatility with greater productivity through specialization. Because the farm economy leads you to a lack of diversification within your business, it is critical to build a separate financial portfolio that is not tied to agriculture. Specialize in agriculture and diversify in your personal portfolio.

Flexibility

The more non-farm assets you own the greater flexibility you have. If you want your heirs to take over the farm, can they afford to pay full fair market value? Can you afford to sell below that price? You have the ability to transfer your farm at lower values when your retirement income is not solely dependent on the sale of farm assets.

Even if passing the farm to heirs is not your concern, you should make selling decisions based on market performance, not on your income needs. A properly structured investment portfolio matches investment time frames with income needs, allowing you to tap into different assets for different purposes.

Remember that when you control your income streams, you also control tax liability. You can determine what taxable income you will have now and in the future.

Track record

There will always be a need for agriculture, but what it takes to remain profitable changes. You will eventually reach the time when expanding your farm is no longer your goal. Farming is a very time demanding business. At what point do you want your assets to be working harder than you are?

There are few arenas that have exhibited a better long-term track record than financial assets. Even with the type of market volatility we have seen recently, there has never been a 20-year time horizon where stocks have lost money.

Over the past 70 years, big company stocks (known as large cap stocks) have averaged over 10% per year. Small company stocks have exceeded 12%. Even corporate bonds have returned about 8%. While none of these are guaranteed, the track record is outstanding, and far exceeds what inflation has been.

(Put in “Growth of Different Investment Since 1925” and “Long-Term Investing May Reduce The Risk Of Owning Stocks” charts)

What Types of investments should you consider?

Before you choose an investment, know what you are looking to achieve by investing. This means setting expectations for *performance* and *risk*. Next you move to an *asset allocation* analysis, and then make the final investment selection within specific asset classes.

Performance

Every financial investment has its own investment performance potential, yet there are only three primary investment aspects with any investment: Safety of Principal, Income and Growth. These are not mutually exclusive, but no one investment can meet all three to a maximum level.

For retirement, you probably want to break your needs down into different time horizons, each with a different performance objective. A general recommendation uses a 0-3 year time frame, a 4-7 year time frame, and then a portfolio segment for income needs that are over 7 years away. Broadly speaking, these time horizons would focus on ‘safety of principal’ (0-3 years), ‘income’ (4-7 years), and ‘growth’ (over 7 years).

Safety of principal refers to the likelihood that the principal will be returned in total at any given time. This ‘liquidity’ is crucial when your funds must be available in a short time frame. A portion of your portfolio should be positioned here. This would include cash reserves, special liquidity needs and sometimes an opportunity fund.

Income refers to the cash flow in interest or dividend that an investment will earn on an ongoing basis. Income is a critical component with a medium term time horizon. It is also crucial for you to look at the difference between cash flow and tax flow.

Growth refers to the potential appreciation or gain that could be realized upon the sale or maturity of the asset. For longer-term goals, growth that outpaces inflation is critical.

Risk

Taken by itself, the word 'risk' sounds pretty negative – not a good thing to do with money. Once it is broken down into what it really means in investing, it is not quite so scary. Most risks can be foreseen and effectively managed.

Inflation risk – Inflation is one of the easiest signs to recognize. The main risk from inflation is failing to outpace it. People refer to that as living on a 'fixed' income. Inflation cannot always be predicted, but there are sensible ways to respond to it. If your savings and investment funds are failing to outpace inflation, you may want to consider a more diversified portfolio including more growth-oriented investments.

Interest rate risk – Some investments tend to be sensitive to changes in interest rates. This is particularly true of bonds. When interest rates fall, bond prices rise. Of course, the opposite is also true. When interest rates rise, the values of existing bonds tend to fall. Shorter-term bonds are less interest rate sensitive. A diversified portfolio can benefit from rising rates (CDs and Money Market funds), falling rates (Bonds), and has some assets not directly tied to interest rates (equity assets).

Economic risk – Some industries and companies adjust to rapid changes in the economy very well. Others, particularly big industrial companies with a lot of large equipment, take longer to react. Since that difference can affect each company's income, it affects the price of the stock as well. Therefore, it is wise to invest in more than on industry.

Market risk – When a market experiences a downturn, it tends to pull most securities down with it. This drop in stock price does not reflect a weakness within the company. It reflects the emotional mood of the investing public. Eventually, the affected securities will recover to market values more closely related to their fundamental strength. So long as the company is sound, its price will eventually recover. Remember that long-term investors are the most successful. The key is to be patient and consistent in your investing philosophy.

Specific risk – If you could pinpoint all the outside influences that will hurt a company you have chosen– unexpected events like drought or political change – you could minimize your exposure by finding another company that would benefit from the same occurrence. Think of all of the rain ponchos sold at Walt Disney World Resorts. People come for the sunshine, but Disney also profits from the rain. Diversification will limit specific risk.

Asset Allocation

There are over 10,000 different mutual funds and countless individual stocks and bonds available to invest in, offering a variety of investment opportunities. While there are bound to be investments that match your objectives, how do choose the right ones for you?

Asset allocation is an investment strategy that seeks to reduce investment risk, while maintaining a desired rate of return, by spreading an individual's investments over a number of asset types. By using historical performance and diversifying your portfolio among several asset classes, you can substantially reduce your risk while still retaining the potential for competitive returns. Asset allocation helps you select the appropriate asset classes for your investment portfolio.

(Insert "How The Efficient Frontier Enhances Your Portfolio")

Proper diversification means more than just owning different asset classes. Many investors have more than two asset classes within their portfolio without being properly diversified. They may have investments in international stocks and bonds, blue chip stocks, cash and real estate asset classes. But no matter how many asset classes they may be spread across, their portfolio may not be efficient.

In this graph, an investor's current portfolio is represented by Portfolio A. Portfolio A lies within the efficient frontier. If this investor could move to Portfolio B on the frontier, he could have the same expected return while substantially reducing his risk (volatility). If he could instead move to Portfolio C, he may then maximize his return while increasing his exposure to risk.

The point is the frontier represents an efficient tradeoff, in which taking more risk yields the maximum expected return.

Most investors have not consciously selected the amount of risk they wish to expose themselves to, nor do they know the return they can reasonably expect to receive.

Over time, financial markets and an individual's goals and situation will change. Periodically, an investor should review his or her situation to ensure that current investment allocations are still appropriate.

Investment Selection

Once you have selected the classes of investments that will best meet your investment goals, you are ready to select specific investments. There are four basic criteria you can use when selecting specific investments:

- Behavioral characteristics – First, examine the behavioral characteristics of the security.

This is where all the statistical analysis comes into play. Look for investments that show a correlation with the expected return for the asset class over a long period of time. Simply put, has it done what was expected of it?

- Liquidity – If you have a major need coming up in a couple of years that will necessitate liquidating a portion of your holdings, will you have easy access to your money without fees? Which assets will generate your income needs? How easy will it be to reallocate these dollars when it is necessary? All of these questions must be addressed before you invest.

- Performance history – Look for investments with a better performance history than the average for their asset classes (peer group). Be aware of what has lead to past performance. Remember to keep comparisons within asset classes.

- Effect of taxes – Examine the effect of taxes on your investment. Are your earnings tax deferred? Does the timing of a capital gain distribution matter to your tax situation? Are you looking to reduce your taxable income by investing in tax-free instruments such as municipal bonds and Roth IRAs? What is the tax status of the withdrawal when you need access to the money?

Specific Asset Classes

Cash Assets – Cash refers to money that is available for immediate needs, emergency use, or to take advantage of opportunities. It is short term maturity assets (less than one year typically) such as checking accounts, savings accounts, money market funds, and Certificates of Deposit. The primary investment objective of cash assets is stability of principal.

Bonds – A bond is simply evidence of a debt. It can be secured or unsecured by the borrowing entity. Bondholders, unlike stock shareholders, are creditors of the bond issuer, rather than owners of the company. The investor loans the money and receives interest in return, as well as the original amount at maturity.

There are three types of bonds:
- U. S. Government (or foreign government)
- Municipal (city or state)
- Corporate

Many factors can affect the value of a bond, including:
- Coupon rate
- Maturity date
- Call or put features
- Market interest rates
- Debtor's financial stability
- Insurance

While bonds offer growth potential in times of dropping interest rates, the primary investment objective of bonds is income.

Stocks – While bonds are instruments of debt, stocks represent ownership. Money is invested directly into enterprises whose value and rate of return may vary. You become a partial owner of the company you invest in. Common shareholders have a residual claim to the corporation's profits (i.e., bondholders and preferred stockholders are paid dividends before common stockholders). Preferred stock represents shares of ownership in the corporation also, but preferred stock dividends are fixed at the time of issuance. Therefore preferred stock prices are inversely related to interest rate fluctuations, much like bonds.

The type of company you choose to invest in will depend upon your investment objective.

A *'Blue Chip'* company is highly esteemed as an investment based on the following criteria: earnings in good times and bad over a long period of time; 25 or more years of paying quarterly cash dividends; and leadership in solid, established industries coupled with solid expectations for continued success.

A *growth company* normally pays little to no dividends, but investors expect the value of the stock to increase dramatically over time. This may be due to a new product being introduced, expansion plans, or just being in a growth industry.

Utility stocks are a popular type of common stock for many investors due to the high dividend income that utilities generate. High income with growth potential makes them attractive investments. The utilities group includes electric light and power, gas distribution and transmission, telephone, telegraph and water.

In any of these cases, the first objective for owning stocks is still growth. That could be growth of the value of the stock itself, or merely growth in the income generated by the security.

Real Estate

Real estate offers a number of opportunities for investors. Similar to investing in stocks, real estate offers appreciation potential and income potential, but it also offers tax benefits. You may choose real estate as a pure investment, in which case you would purchase it through Real Estate Investment Trusts (REITs), Limited Partnerships or other managed portfolios; or you can purchase it directly, at which point it becomes a business venture. The difference between these two options is the amount of time you are willing to put in, and the amount of risk you wish to take.

You also can get into real estate as a debt instrument by investing in mortgages.

Other assets

There are other investment categories, such as precious metals and collectibles. They may be an intelligent hedge for your portfolio, but these are normally best purchased only after speaking with a trained professional who totally understands your financial situation.

How should you own these investments? (Ownership Form)

Once you have selected the types of investments you want to own, you must next decide what ownership form to use. As a small business owner, you can own your investments either inside or outside your company.

Inside Your business

The entity type you choose for your business will determine what options are available to you. All businesses can establish a qualified pension plan.

Pension Plans

Profit sharing plans allow you to shelter up to 15% of your income into a retirement plan. The contributions are tax deductible, and the earnings accumulate tax deferred. SEP-IRAs are popular choices since they offer both low costs and multiple investment options.

Money purchase plans allow you to contribute up to 25% of your income into a retirement account. This 25% can be all through a money purchase plan, or split 10% in a money purchase with the other 15% in a profit sharing plan. With a money purchase plan, contributions are required each year.

Certain types of pension plans (Target Benefit and Defined Benefit for example) actually allow you to shelter far greater percentages of your income, dependent upon your age and retirement date. Talk to a pension specialist before beginning one of these plans.

For many small businesses, SIMPLE IRAs offer an attractive alternative. Here you can shelter the lesser of 100% of your income or $6,000. There are other criteria that must be considered if you have employees, but overall the SIMPLE IRA has been a great success since its introduction.

Each type of pension plan has eligibility requirements, vesting schedules, as well as potential required matching contributions. You ought to review all pension options with your investment and tax advisors before selecting the plan for you.

Non-Qualified Deferred Compensation

While pension plans must be non-discriminatory (essentially the same) for all employees, non-qualified deferred compensation plans are individually negotiated. A deferred compensation agreement postpones payment for currently rendered services until a future date, with the effect of postponing taxation until the compensation is received.

Employers use this type of plan to provide benefits in excess of the limitations placed on qualified plans. The type of business entity you have will determine how the dollars are treated in the case of owners, but should not make a difference for other employees.

Any deferral must be agreed upon before the compensation is earned. The terms of this deferral must be laid out in detail.

Outside Your Business

Just as you have options of pension plans or non-qualified plans within your business, you have similar choices with personally owned investments.

IRAs

IRAs are the personal alternative to a full pension plan. Any person under the age of 70 ½ who has earned income can use an Individual Retirement Account (IRA). The maximum allowed is the lesser of $2,000 or 100% of earned income for an individual. If the wage earner is married, an additional $2,000 may be contributed on behalf of a lesser earning (or non-working) spouse, using a 'spousal' IRA account.

Traditional IRAs

Contributions are normally tax-deductible (your tax advisor can assist you in determining your tax deductibility), with all growth being tax-deferred. Withdrawals are taxed as ordinary income. (If you have made non-deductible contributions, those contributions are received tax-free when withdrawn.) Deductibility is based on your earned income, and whether or not you or your spouse is covered by another pension plan.

Distributions made prior to age 59 ½ are subject to a 10% Federal penalty (as well as a state penalty in Wisconsin) unless:

- Made due to death or disability
- The distribution is rolled over into another IRA
- Made as substantially equal periodic payments over the life of the IRA owner, or the joint lives of the owner and a designated beneficiary
- Made for certain medical payments (and potentially for health insurance)
- Made for certain "qualified higher education expenses"
- Made for "qualified first-time home buyers"

Distributions must begin at age 70 ½. Failure to take your minimum distribution results in substantial penalty taxes. Minimum distributions are calculated on the life expectancy of the taxpayer. By adding a direct beneficiary, you can stretch your distributions out over a much longer time frame, reducing the amount you need to claim each year. Minimum distribution rules are very complex. Who you choose as your beneficiary, and how you calculate the minimum distributions can have a dramatic impact on the way your heirs are taxed at your death. This is an area where a competent tax advisor can save you money.

Roth IRAs

Beginning in 1998, taxpayers have a new, tax-favored retirement accumulation vehicle in the Roth IRA. Similar in concept to the traditional IRA, the Roth IRA differs in that contributions are never deductible, and, if certain requirements are met, 'qualified' distributions from the account may be received free of income tax. Qualified distributions are made:

- After the taxpayer reaches 59 ½
- In the event of the taxpayer's death

- Because the taxpayer became disabled
- To pay for "qualified first-time home buyer" expenses.

You can either open a Roth IRA as an active account (the lesser of $2,000 or 100% of earned income), or as a conversion account. Traditional IRAs can be converted to a Roth IRA by taxpayers with an AGI (Adjusted Gross Income) of $100,000 or less in the year of conversion. (Converted amounts are <u>not</u> included in determining if AGI is $100,000 or less.

The conversion from the traditional IRA to the Roth IRA is a taxable event. Converted taxable amounts (all IRA contributions that were previously deducted along with all tax-deferred growth) are added to the taxpayer's income in the year of the conversion.

In an industry with volatile profits, Roth IRA conversions can be a wonderful way to average out your income from year-to-year. Simply use deductible IRAs in high-income years, and convert to a Roth in low-income years. Active contributions can go into a Roth IRA in the lower income years.

Converting IRAs to a Roth can also be an effective estate-planning tool.

You need to talk to your financial and tax advisor before considering a Roth conversion.

Non-Qualified Assets

Simply put, all other investments you own fit this category. This is the first way most people invest. Assets are titled in your name, and are fully included in your estate. The way your assets are titled will affect how they are taxed, both from an income and an estate basis.

What asset form should you use?

Your final decision relates to the asset form in which you will own your investments. In general that means either owning individual securities, or using managed portfolios.

Individual Securities When you own individual securities, you pick specific securities (stocks or bonds) for your portfolio. You can actively manage your account to meet your specific needs for income, growth and tax planning. For many clients, this is a pastime they enjoy. Active management does take time.

Other clients will use a portfolio manager to construct an individual portfolio. The portfolio should be designed for the individual client, taking into account income, growth and tax needs.

Managed Portfolios For most investors, managed portfolios are the way to invest. While you lose individual control, you usually gain lower costs and ease of investing. Managed portfolios take very little of your time.

Mutual Funds offer investors the opportunity to pool their dollars into a larger buying unit, with professional management to oversee the portfolio. There are money market funds, corporate bond funds, municipal bond funds, growth and income funds, growth funds, international and global funds, balanced funds and sector funds. Each has its own performance objectives and management style.

Mutual funds are always purchased from and sold back to the issuing company. There is no secondary market. You must receive a prospectus when you purchase a mutual fund.

Mutual funds can be excellent investments for beginning investors and sophisticated investors alike. However, with so many funds from which to choose, the decision process can be challenging. There is a quality control checklist at the end of this chapter that will help you streamline the process in making your final fund decisions.

Unit Investment Trusts (UITs) are similar to mutual funds in that they are pooled investments that generally invest in tax-exempt bonds, corporate bonds, utility stocks, or government-backed mortgages. Unlike mutual funds, unit investment trusts hold onto their original securities for the life of the trust instead of trading them. Also, unlike mutual funds, UITs are traded on a stock exchange.

Limited Partnerships pool the monies of several investors to purchase income-producing properties. When the partnership subsequently receives income from these properties, it passes the income on to its investors as dividend payments. When the partnership sells a property, any capital gains are passed along to investors with their principal. Among common types of limited partnerships are real estate, equipment leasing, oil and gas, and historic property rehabilitation partnerships. Unlike mutual funds that issue a 1099 for tax records, partnerships issue a K-1.

Real Estate Investment Trust (REIT) works like a cross between a mutual fund and a limited partnership. REITs pool the money of many investors to buy income-producing properties, write mortgages on existing buildings, or both. They are usually traded on a stock exchange or over the counter like regular stocks.

Annuities are investment contracts between an insurance company and an investor. The contract is purchased either with a single payment or with a series of payments. While the funds are in the annuity, they grow tax-deferred. Under current law, withdrawals from the annuity prior to annuitization will be considered as though interest comes out first and the return of investment contribution second.

With a variable annuity, the cash value of the annuity will fluctuate with changes in the performance of the underlying investment portfolio. Variable annuities are sold by prospectus only. The prospectus contains important information concerning charges and expenses.

Life Insurance is a unique asset. Because of its potential high yield and tax favored benefits, it can be used to solve some of life's perplexing financial problems. It can be used to:

*create an estate
*pay death taxes and other estate settlement costs
*fund a business transfer
*build a college fund for children (or grandchildren)
*pay off a mortgage or other debts
*protect a business from the loss of a key employee
*create a retirement fund
*replace a charitable gift
*equalize inheritances.

Whole life insurance

Whole life insurance, sometimes called "permanent insurance" or "ordinary life", is designed to stay in force throughout one's lifetime. It is a type of policy well suited to needs that do not diminish over time, such as paying estate settlement costs. Generally, the annual premiums for this type of policy remain the same throughout the life of the insured. During the early years of the policy, the premiums are higher than those of a straight term life policy. As time passes, the level premium, combined with a build-up of cash values, keep whole life policies in force. By contrast, the premiums on term life policies typically become relatively high, and many term policies are allowed to lapse.

Variable life insurance is similar to whole life in that the premium payments are level, and there is generally a minimum guaranteed death benefit. Unlike whole life policies, however, variable life policies permit the policyholder to allocate a portion of each premium payment to one or more investment options after a deduction for expense and mortality charges. The death benefit and cash value of a variable policy increase and decrease based on the performance of the investment options chosen. Because of the investment options inside a variable policy very often involve marketable securities (e.g., stocks, bonds, and money market funds), the Securities and Exchange Commission requires this type of policy to be accompanied by a prospectus.

Universal life insurance contracts differ from traditional whole life policies by separating the "protection element", the "expense element", and the "cash value element". Dividing the policy into these three components allows the insurance company to build a higher degree of flexibility into the contract. This flexibility allows (within certain guidelines) the policy owner to modify the policy face amount or premium in response to changing needs and circumstances. Because of these internal charges against the "cash value element" of the policy, complete disclosure of the charges is provided to policyholders in the form of an annual statement.

Variable Universal life insurance contains a combination of features found in "variable life" and in "universal life" policies. As with universal life contracts, the owner of the policy can (within certain guidelines) modify the policy death benefit and change the amount and timing of premium payments to meet varying circumstances. The most prominent feature of the variable universal life contract is the policyholder's ability to direct where net premiums will be invested. Once the costs for insurance protection and company expenses are met, the balance of the premium goes directly into investment options selected by the policyholder. Typically he can choose between growth stock funds, bond funds, money market funds, international and global funds, balanced accounts and a fixed account.

As with other permanent life insurance contracts, the owner can borrow against the cash values of the policy. The interest rate charged on borrowed funds is generally lower than open market rates; with some companies having a zero net interest charge. Surrenders and loans can often be made on a tax-free basis.

An individual considering this type of policy should refer to the prospectus for detailed information regarding the policy being offered.

Quality Control Checklist Questions:	**Yes**	**No**
Do the objectives of the fund you are considering meet your personal investment objectives?	___	___
Have you emotionally committed to leaving your money in this investment long-term, through the ups and downs of the market?	___	___
Is the fund you are considering part of a "family of funds"?	___	___
Have you reviewed the fund's 1, 3, 5 and 10-year track records?	___	___
Is the current portfolio manager the same manager who produced the track record you reviewed?	___	___
Is the investment philosophy of the fund the same today as it was:		
5 years ago?	___	___
10 years ago?	___	___
Have you reviewed the Management costs associated with the fund?	___	___
Marketing costs	___	___
Acquisition costs	___	___
Liquidation costs	___	___
Do you have the privilege of telephone exchanges between your funds?	___	___
Is there a cost for exchanges?	___	___
Is a specified time frame required to elapse between exchanges?	___	___

Have you investigated the fund's reputation for investor services? ___ ___

Is cost/tax basis tracking provided? ___ ___

Is your performance reported to you? ___ ___

Have you investigated the tax aspects of this fund? ___ ___

Do you know your investment time horizon? ___ ___

Do you know your risk tolerance? ___ ___

Do you know what you will do when:

The market falls? ___ ___

The market rises? ___ ___

Do you know the type of investment counseling/advice you will get? ___ ___

Chapter 6

Techniques for Managing My Estate during My Life-Time

For a variety of reasons, you may want to delegate the management of your financial affairs and/or health care to others during your lifetime. You may want to simply devote your energy to other matters. Or, you may want to be prepared for your own disability brought on slowly by a disease or by aging, or more suddenly by an accident, stroke or other health problems. This chapter discusses several legal arrangements that can be created to delegate as much or as little authority as you choose.

Durable Power of Attorney for Financial Matters

A durable power of attorney for financial matters gives another person legal authority to transact financial and other business matters for you. The purpose of giving another person this power is to allow him or her to conduct your financial affairs when you are not able to do so due to a temporary or permanent incapacity.

The power is usually made effective at the time you sign the power of attorney. This means that your agent can act for you even while you have the capacity to act for yourself. By making the power effective immediately, you avoid the complication of defining a triggering event, such as your incapacity, to make the power effective. Being effective immediately also allows your agent to act for you when it is simply a matter of convenience, such as paying bills while you are on vacation.

The durable power of attorney is effective only while you are alive. Upon your death, the power terminates and the disposition of your assets will be controlled by your revocable living trust or will. If you do not have a revocable living trust or a will, your assets will be distributed according to the rules of intestate succession under Wisconsin statutes.

Your durable power of attorney for financial matters can be written broadly to include all of your financial matters, or it can be limited to specific financial matters. Powers that are often specifically mentioned include:

- Power to invest, lend, borrow or otherwise manage money.
- Power to buy, sell, lease or mortgage property.
- Power to commence or defend legal actions.
- Power to deposit and withdraw funds in or from any financial institution.
- Power to exercise your rights as a shareholder or bondholder, such as to vote in shareholder meetings.
- Power to sign and file income tax returns and other government reports, applications, requests and documents.
- Power to enter your safety deposit box.
- Power to make gifts.
- Power to disclaim property that you inherit.

Many people name their spouse and one or more children as their agent. Another family member or trusted friend can also be named. A durable power of attorney for financial matters can give you the peace of mind that your financial affairs will not be held up because no one has authority to act on your behalf.

Health Care Power of Attorney

A health care power of attorney gives another person legal authority to make your health care decisions if you are incapacitated. Unlike the durable power of attorney for financial matters discussed above, your agent for health care matters will have no power to act unless two doctors determine that you are no longer able to make your health care decisions.

Your health care power of attorney can give your agent the power to make decisions about your care in the event of terminal illness or a persistent vegetative state. It can give your agent the authority to withdraw life support, including tubes for nutrition and hydration. You should fully explain your wishes to your agent so that he or she knows what to do regardless of the circumstances that arise.

The Wisconsin legislature requires the use of a specific form for the health care power of attorney if you want your agent to have the authority to place you in a nursing home for long-term care. This is an extremely important right because it eliminates the need for the court to nominate a guardian for you.

A guardianship is expensive and often complicated. It is also slow, often at a time when speed to act is important. The proposed guardian usually hires an attorney to prepare court documents and attend court hearings. The Wisconsin Department of Health and Family Services gets involved to investigate and prepare a study. The court appoints a guardian ad litem to investigate and determine your best interests. The court then determines what assets you and your spouse own and requires your guardian to prepare an annual account of your assets—including your annual income and expense.

Business Arrangements

There are several legal entities that can be used to organize a business. The choice of business entity affects the amount of taxes you pay, your liability for business debts, the management of the business and the ease of transferring the business to another owner. This section briefly describes the non-tax characteristics of the most common entities. The next section discusses the taxation of these entities.

Sole Proprietorships One person who has full control of and responsibility for the business owns a sole proprietorship. The sole proprietor can hire managers but is ultimately responsible for all management decisions. A sole proprietor is liable for all of the debts of the business. There are no restrictions on the sole proprietor's right to sell the business. There are no agreements or formalities required to form a sole proprietorship.

General Partnerships A general partnership has two or more owners who are carrying on a business and who share profits or losses. Each partner can be held liable for the full debts of the partnership if the partnership is not able to pay its debts. The partners can all participate in management and each partner can bind the partnership to contractual obligations. If they choose, partners can delegate the management of the business to one or more partners or to outside managers.

A partner is free to sell his or her partnership interest at any time. However, sale of an interest in a partnership will generally result in a dissolution of the partnership unless the remaining partners and the new partner agree to continue the partnership. A general partnership agreement does not have to be in writing.

Limited Partnerships A limited partnership has at least one general partner and at least one limited partner. The general partners are liable for the full debts of the partnership and have the rights and responsibilities of partners in a general partnership discussed above. Limited partners are <u>not</u> liable for the debts of the partnership unless they have personally guaranteed the partnership debt or are liable as a result of an individual action other than being a limited partner.

Limited partners are not allowed to participate in the management of the partnership business. Sale of an interest in a limited partnership will usually result in a dissolution of the partnership interest. A limited partnership must have a written partnership agreement that is filed with the Secretary of State.

Limited Liability Companies A limited liability company is a relatively new form of doing business in the United States. Most states have adopted limited liability statutes in the last few years. The limited liability company (LLC) is formed by filing articles of organization with the Secretary of State. Most states require that there be two or more members (owners) of the LLC. Wisconsin allows only one member to form an LLC. Members are <u>not</u> liable for the debts of the LLC unless they have personally guaranteed the LLC debt or are liable as a result of an individual action other than being a member of the LLC. Therefore, each member's loss as a result of investing in the LLC is generally limited to the amount he or she paid for the membership interest.

The management of the LLC, transferability of members' interest in the LLC and the continuation of the LLC in the event of the death of a member or sale of a membership interest can all be specified in the articles of organization.

Corporations A corporation is formed by filing articles of incorporation with the Secretary of State. There can be one or more shareholders (owners) of the corporation. The shareholders elect a board of directors who hire officers to manage the corporation. In a closely held corporation, the shareholders usually elect themselves as directors and hire themselves as officers.

Shareholders are not liable for corporate debts unless they have personally guaranteed the corporate debt or are liable as a result of an individual action other than being a shareholder. Therefore, shareholders generally have no more at risk than they invested in the corporation.

The life of a corporation is generally perpetual. Therefore, if a shareholder dies or sells his or her shares, the corporation continues unless a majority of the shareholders agree to dissolve the corporation.

Some restrictions can be placed on the right of a shareholder to sell shares of stock, but shareholders must have the right to sell. For example, shareholders can be required to first offer their shares to the corporation or other shareholders before selling them to another party.

Trusts A trust is established when a grantor (the person setting up the trust) writes a set of instructions telling the trustee (the person or entity that agrees to carry out the terms of the instructions) how to deal with the assets placed in the trust for the benefit of the beneficiaries (the person or persons who receive income and/or corpus from the trust). Given this broad latitude, trusts can be used for many different purposes--including operating a business.

If the trust is irrevocable, the terms for operating the business that are set out in the trust document cannot be changed. If the trustee is given complete discretion in operating the business--including buying and selling business property, then the trustee is free to do whatever it deems in the best interest of the beneficiaries. If restrictions are placed on the trustee, such as a prohibition from selling farmland, then the land cannot be sold even if circumstances change and the grantor wishes the land would be sold.

If the trust is revocable, the grantor can change the terms of the trust at any time. As discussed below, the tax consequences of a revocable trust are significantly different from those of an irrevocable trust.

Hybrid Organizations Businesses can be organized by combining two or more of the above organizations. For example, a corporation can be formed to own the operating assets and to carry on the primary business activities. A limited liability company could be formed to hold the land that is used in the business. The corporation can rent the land from the limited liability company.

The organizations can also be layered. For example, a corporation could be formed to be the general partner in a limited partnership. Or, one corporation could own shares of another corporation.

Tax Implications

This section will discuss the effect of the various business organizations on the owner's income tax and social security tax liability. Estate and gift taxes are covered in the next chapter.

Sole Proprietorships The owner of a sole proprietorship pays both income taxes and self-employment taxes on the net income of the business.

Partnerships (General and Limited) A partnership is not a tax paying entity. It reports its income and deductions on a Form 1065 and allocates the income and deductions among its partners. Partners report their share of income and deductions on their individual returns. A complex set of tax rules prevents taxpayers from shifting income into lower tax brackets by transferring the income to another partner through the partnership.

Partners pay self-employment tax on their share of the partnership income.

Generally, transferring an asset to the partnership in exchange for an interest in the partnership does not trigger recognition of gain or loss. Similarly, transferring an asset from a partnership to a partner for an interest in the partnership does not trigger recognition of gain or loss. In both cases, the income tax basis of the asset is carried over.

> *Example 1*
> If a partner contributes land with an income tax basis of $50,000 and a fair market value of $600,000 to a partnership, no gain is recognized. The partnership has a $50,000 basis in the land.
>
> If the land is distributed back to the partner, no gain is recognized. The partner has a $50,000 basis in the land.

Limited Liability Companies The object of most limited liability companies is to be taxed like a partnership. Tax regulations that became effective on 1 January 1997 allow LLCs to choose how they will be taxed.

LLCs with two or members will be taxed like a partnership unless the LLC elects to be taxed like a corporation.

LLCs with only one member will be taxed as a sole proprietorship of the owner unless it elects to be taxed as a corporation.

Corporations Under the general rule, a corporation is a tax paying entity. It reports its income and deductions on a Form 1120 and pays tax on its net income. Salaries, rent and fees paid to shareholders are deducted on the corporate tax return and are reported as income on the return of the shareholder that receives the payment. By contrast, the corporation does not deduct dividends paid to shareholders and the shareholder still has to report the dividend as income.

Wages paid to a shareholder are subject to the FICA tax.

Similar to partnership taxation, assets can be transferred to a corporation in exchange for shares of stock without recognizing the gain or loss on the asset, if some additional requirements are met. However, transferring an asset from the corporation to the shareholder will trigger recognition of gain for both the corporation and the shareholder.

> *Example 2*
> If land with an income tax basis of $50,000 and a fair market value of $600,000 is transferred to a corporation in exchange for shares of stock, no gain is recognized if other requirements are met. The corporation has a $50,000 basis in the land.
>
> If the land is distributed back to the shareholder in exchange for the shares, both the corporation and the shareholder must recognize $550,000 of gain.

S Corporation A corporation that meets the qualifications can elect to be taxed under subchapter S of the Internal Revenue Code. Those rules treat the corporation as a conduit for the business income and expenses. The shareholders are required to report their share of the income and expenses on their individual returns. The corporation does not pay tax on the income.

Trusts The taxation of income earned by a trust depends upon the type of trust and whether or not the income is distributed to the beneficiaries of the trust.

If the trust is revocable (the grantor can revoke the trust) then the income is taxed to the grantor whether it is kept within the trust or distributed. In effect, the trust is ignored for income tax purposes. All the income is taxed to the grantor as if he or she still owned the assets outright.

If the trust is irrevocable, then the income will be taxed to the trust if it is accumulated in the trust or to the beneficiaries if it is distributed to the beneficiaries in the year it is earned.

Chapter 7

Distributing my Estate

Developing an Estate Plan

A well-developed estate plan assures that your goals and objectives continue to move toward accomplishment after your death. Without an estate plan, the state laws will decide who inherits your estate, without regard to your personal wishes or the special needs of your family.

As a farmer, you are likely to have the following basic goals, which should be considered in your estate plan:

Financial Security

You will want to provide the structure for your family's continued financial security and opportunities, especially your surviving spouse and any dependent children. You also will want to protect your estate from preventable risks, such as third-party claims, debts and the costs of potential long-term care.

Farm Transfer to Next Generation

If any of your children want to continue the farm ("*on-farm heirs*"), you will want to give them that opportunity, without their being burdened with excessive debt or cash flow problems.

Treat Children Fairly

After recognizing the past contribution of commitment and effort by any on-farm heirs, you will want to treat all your children fairly, which may not necessarily be equally.

Avoid Income and Estate Taxes

You will want your estate plan to limit income taxes during your life and the lives of your heirs and to avoid estate taxes, to the greatest extent possible.

Limit Probate

You will want to limit the delays and expenses of probate, to the greatest extent practical.

The Role of the Estate Plan in Transferring the Family Farm

Throughout your life, you have planned, worked and committed most of your estate to building a successful farm. If the next generation wants to take over your farm, your succession plan should begin the transfer before your age makes your death likely. However, your estate plan can provide an effective structure for transfer of the farm in the event of your untimely death. A good estate plan will effectively balance the income needs of your spouse and any dependent children, and the needs and desires of your "*on-farm*" and "*off-farm*" heirs. Often, your Will (or Living Trust) will include bequests or purchase options that make it feasible for interested family members to successfully continue and improve your family farm.

Farm-purchase planning requires an objective assessment of your family's ability to continue the farm and to meet the ongoing financial obligations of a farm purchase. You may consider special bequests, price discounts and favorable payment terms to recognize the past contribution of continuing on-farm heirs when setting the price and terms for a farm transfer.

Advisors for Your Estate Plan

Changes in agriculture have placed a premium on the assistance of advisors with substantial knowledge and experience about the unique problems facing today's farmers. Your estate planning advisors will usually include an attorney experienced in farm estate and tax planning, your farm accountant, and often, an insurance agent or financial planner. The key to selecting any professional advisor is that advisor's reputation in the agricultural community.

Gift and Estate Taxes

Estate and gift taxes ("*Transfer Taxes*") can be avoided, or at least limited, through estate planning. The Federal estate tax rates rise from 37% at $650,000 in 1999, to 55% at $3 million. The Wisconsin estate tax rates rise from 4% at $650,000 in 1999, to 9.6% at $3 million and can be as high as 16%.

In order to determine whether you are at risk for estate taxes, you must first determine the value of your estate. All assets that you own are subject to estate taxes, including your Individual Retirement Accounts and other retirement plans and the proceeds of any life insurance policies which you own. You should take the time to prepare, or have your accountant prepare, a complete financial statement, since the value and nature of your estate is the basis for beginning your estate plan.

Methods for Reducing Transfer Taxes

The Transfer Tax system itself provides certain opportunities to minimize gift and estate taxes. Your estate plan advisors may use any one or more of these methods to eliminate, or at least, reduce your gift and estate taxes.

Method 1: Lifetime Giving Programs

The proper gifting of an asset to a third party excludes the asset and its future growth and appreciation from the donor's estate. Gifting can effectively remove from your estate assets that are otherwise vulnerable to taxation. If you are at risk for estate taxes, your plan may include gifts during your life of assets that tend to increase in value or which facilitate the eventual transfer of the family farm to the next generation.

During 1999, the first $10,000 of gifts by a donor to any other person is not included in the donor's total gifts during that calendar year. This annual exclusion amount for following calendar years is indexed for inflation and will rise annually. Also, spouses may consent to split their gifts allowing the transfer of both annual exclusions amounts to a donee ($20,000 per donee in 1999). The annual exclusion is not allowed for future gifts of interests in property. However, with proper planning, assets can be gifted to trusts for the benefit of your spouse, children or other heirs with use of your annual exclusion amount. Such trusts may hold life insurance, farm real estate or other assets, which are then available for the benefit of your heirs but excluded from estate tax upon your death. Outright gifts are often used to facilitate the transfer of the family farm.

Charitable giving is also an effective tool for minimizing income taxes during your life and estate taxes upon your death. Charitable giving will be further discussed in a later section.

Method 2: The Unlimited Marital Deduction

Under both the federal and Wisconsin marital deduction rules, you can transfer any value of assets to your spouse, if an U.S. citizen, without estate tax. Your spouse can then continue planning actions during his or her life. If your combined estate is less than the surviving spouse's Unified Credit, he or she can receive the estate and distribute it at his or her death. However if the value of your spouse's estate is still larger than his or her Unified Credit, the estate tax is not avoided but merely deferred until your spouse's death.

Method 3: Unified Credit

Under both federal and Wisconsin laws, each person is given a credit against gift and estate taxes or any combination of these Transfer Taxes. This is known as the "*Unified Credit*". In 1999, your Unified Credit is sufficient to allow you to transfer up to $650,000 of assets to third parties without gift or estate taxes. While the Unified Credit increases annually through the year 2006, you must recognize that your estate may also increase through appreciation.

Annual Changes in the Gift &
Estate Tax Exemption Equivalent

1999	$ 650,000
2000	$ 675,000
2001	$ 675,000
2002	$ 700,000
2003	$ 700,000
2004	$ 850,000
2005	$ 950,000
2006	$1,000,000

If you are married and you anticipate your estate will exceed the exemption equivalent in any year, your Will (or Living Trust) should include provisions to allow the Unified Credit to be applied, to the extent necessary, in both you and your spouse's estate. With proper planning, up to $1.3 million in 1999 can be transferred to your heirs free of estate tax.

The Wills (or Living Trusts) of married couples may include a Family Trust which permits the use of the Unified Credit of the first spouse to die. The Family Trust can permit the Trustee to use the Trust's net income and principal for the health, support and maintenance of the surviving spouse and, if you desire, of your issue. Upon the surviving spouse's death, the Family Trust's remaining assets can then transfer to your heirs, without being taxed in the surviving spouse's estate. Only the surviving spouse's separate assets are then subject to estate tax upon his or her death.

Method 4: Obtaining the Stepped-up Basis

Since January 1, 1986, Wisconsin couples may elect to hold their property as marital property or in joint tenancy or as tenants in common. Certain property, if held as marital property, receives a special tax benefit when a spouse dies. The basis of both the deceased spouse's and surviving spouse's interests in such property changes to its value as of the date of death. This increase in basis is especially beneficial to farmers, since it applies to assets such as real estate, equipment, livestock, and feed. This means that, if the surviving spouse continues farming, depreciation can again be taken to formerly depreciated assets. It also means that benefiting assets may be sold by the surviving spouse or other heirs and gain will only be reported if the sale proceeds exceed the value as of the date of death.

Most farm couples will benefit by classifying their property as marital property, rather than holding it individually, as joint tenants or as tenants in common. Property can be classified as marital property by changing the title on an asset or through a Marital Property Agreement.

Method 5: Special Farm and Small Business Estate Tax Benefits

In order to provide estate tax relief to farmers and other small businesspersons, federal and state laws have been enacted to provide estate tax relief so that farms and other businesses will not have to be liquidated to pay excessive estate taxes. Your advisors should consider the following opportunities and other techniques that are available.

Business Estate Tax Exclusion

The estates of qualified farmers can deduct up to $675,000 of a qualified family business interest (QFOBI) from the decedent's gross estate. This deduction can be combined with the applicable exclusion amount so that a maximum of $1.3 million could be transferred by a decedent's estate free of estate tax. However, the QFOBI is subject to very strict qualification requirements. Further, the qualified heir becomes subject to a recapture of the avoided estate tax if the heir or a member of his family does not materially participate in the farm business for at least five years of any eight-year period within ten years following the decedent's death. In order to take advantage of these combined exemptions, business owners must carefully plan and meet the many technical requirements.

Estate Tax Deferral

If 35% or more of your gross adjusted estate is composed of your farm or other closely-held business interests, your estate may be entitled to pay estate taxes later than the usual nine month deadline. Only interest on the taxes would be due until the fifth anniversary of this deadline, with the balance payable in ten equal annual installments at an interest rate that can be as low as 4% on the tax arising from the first million dollars of interest.

Method 6: Buy-Sell Agreements

As part of your succession plan, family members, partners or key employees may acquire ownership interests in your farm during your life. Your farm may be operated as a partnership, limited liability partnership, limited liability company or corporation. With multiple owners, a Buy-Sell Agreement becomes critical to maintain the closely-held nature of the farm, and to establish the method for transfers of interests between the owners, when an owner retires, becomes disabled, or dies. A Buy-Sell Agreement also serves to assure a buyer for your ownership interest while providing a plan for the orderly transfer of management and control. Life insurance policies are often purchased and bound to the Buy-Sell Agreement to assure adequate funds are available to purchase a deceased owner's interest.

Your Estate Planning Documents

At a minimum, your estate plan will require legal documents to permit ongoing financial management, making of health-care decisions, in the event of your incompetence, and the creation of marital property interests and a Will or Trust to provide for disposition of your estate, upon your death. Today, more than just a Will is required to protect and effectively transfer your estate.

Durable Powers of Attorney

While death is inevitable, you must recognize that a period of prolonged incompetence often precedes death. One out of every two Americans will suffer a period of disability of 90 days or more.

Through your Durable Power of Attorney ("*DPOA*"), you can designate an agent or agents, and alternate agents with authority to manage your financial affairs during any periods you are incompetent. You retain the right to revoke or amend your DPOA at any time. Your DPOA provides a flexible alternative means for dealing with your financial and personal decisions. If you become incompetent without a DPOA, your family's only recourse will be to petition the Court to appoint a guardian. Your family may find the guardianship procedure to be cumbersome, time-consuming and costly.

In a DPOA, your agent's authority continues despite your incompetence. You can designate your agent's power to be immediately effective or to "*spring*" into existence, if you become incompetent. In your DPOA, you can grant your agent broad authority or limit it to specific duties. Your DPOA should be drafted to meet your specific needs.

Most critically, your agents must have earned your trust and confidence, and also should have adequate experience, knowledge and understanding of your goals and objectives.

Powers of Attorney for Health Care

Your desires about medical care are extremely personal based on your philosophy of life, religion and ethics. Today, you must recognize the substantial possibility that your family will be faced with critical decisions about your final medical care, including whether to authorize the withdrawal or withholding of artificial life support. Although you wish to live and enjoy life as much as possible, your family may be faced with decisions regarding health care that would only postpone the moment of your death from a terminal condition or that would only prolong your life if you have a permanent loss of consciousness.

Your Health Care Power of Attorney ("*HCPOA*") permits you to designate an agent and alternate agents to make your medical decisions when you are unable. Your HCPOA should specifically define the scope of the agent's authority and express your desires about specific health care procedures, especially in the life-support area. While the Wisconsin legislature created a "*Statutory*" HCPOA, you may consider having your estate planning attorney draft a HCPOA more particularly expressing your individual health care desires.

Marital Property Agreements

For married couples, the Marital Property Agreement is the key document for determining a married couple's legal position under Wisconsin's Marital Property Act. Your Marital Property Agreement offers substantial income tax benefits and can assist in passing your estate without probate. Married couples may "*opt in*" to, or "*opt out*" of, the Wisconsin Marital Property Act. Through a Marital Property Agreement, couples can agree that property is owned as marital property or individual property by merely stating their election. In addition, couples can agree "*... that upon the death of either spouse, any of either or both spouses' property, ..., passes without probate to a designated person, trust or other entity by nontestamentary disposition...*". Wis. Stats. §766.58(3)(f)

Wills (or Living Trusts)

The basic document in your estate plan is your Will or Living Trust. You will want to establish a plan for the ongoing management and disposition of your estate that will guarantee that your estate transfers to the heirs you seek to benefit in the proportions and manner that will help them the most, with the smallest possible financial or emotional cost. You will want to name Personal Representatives or Trustees who are capable of caring out your wishes after your death. You will also want to recognize and provide for the special needs of your family.

If you are married, your Will or Living Trust can assure the maximum benefit of the Unified Credits available to both you and your spouse's estate. It can assure that a bequest to the surviving spouse, whether in trust or outright, qualifies for the unlimited marital deduction.

Parents and grandparents are often concerned that inherited sums may stifle a child's initiative and deprive the child of the pleasure and satisfaction of self-achievement. If a young child or grandchild will inherit from you, you will want to hold his bequest in trust until he has reached sufficient maturity to individually manage his inheritance. Such trusts can authorize the Trustee to make distributions for appropriate purposes, such as education and if necessary, for support and maintenance. You can include carefully considered guidelines to guide the Trustee's decisions. If you are a parent with young children, you will want to designate appropriate guardians.

In your Will or Living Trust, you may also wish to deal with the needs of handicapped children or other handicapped heirs, gifts to charities, and other personal situations and estate planning objectives.

Irrevocable Trusts

If you are single and your estate exceeds $650,000 in 1999 or if you are married and you and your spouse's combined estate exceed $1.3 million, you may be subject to estate tax. In such estates, Irrevocable Trusts are often established to receive lifetime gifts benefiting from the annual gift tax exclusion. Such gifted assets and their appreciation are then excluded from the estate and ultimately estate taxes.

For example, life insurance that is owned by the insured or payable to the surviving spouse or insider’s estate will ultimately be subject to estate taxes. But life insurance policies obtain most of their value at death and their proceeds may be intended to pay estate taxes. Therefore, it is especially unfavorable to have the life insurance proceeds reduced by the estate taxes. By transferring the policies to an irrevocable trust, the proceeds can be obtained free of estate taxes.

Family Limited Partnerships

Family limited partnerships and limited liability companies have been popular estate planning tools for estates subject to estate taxes. When properly structured, they allow gifting of business and real estate interests by a donor or donors to donees, while permitting the donor or donors to maintain a desired lifetime level of control. The FLAP or LL. holds the assets and income like a business, with the donor and intended beneficiaries acting as partners in the operation of the assets. As general partner or managing member, the donor has active control and can receive necessary income. As limited partners or non-manager members, the donees have no direct management or voting rights. Because of their minority interest and lack of control, gifts of interests to donees may be discounted for gift tax purposes. Because of the complexities of tax laws, planning in this area requires experienced professional advisors.

Wills or Living Trusts: An Objective Explanation

Living Trusts have been highly promoted as the ultimate method for planning estates to avoid probate and estate taxes. Before electing to use a Living Trust, it is important that you have a basic understanding of how they work and what they can do or cannot do.

What is a Living Trust?

All trusts are written agreements that provide for the management of property. A Living Trust is a revocable trust created by an individual or married couple (usually called the "*Grantor(s)*"). During the Grantors' joint lives, they generally serve as Trustees of the Trust, retain the right, at any time, to withdraw the Trust's income and principal, to receive income and principal for their support, maintenance and health and to amend or revoke the Original Trust.

After a married Grantor's death, the couple's Living Trust continues to receive, manage, and/or distribute the Trust estate for the benefit of the surviving Grantor and/or the Grantors' heirs, under the direction of the Successor Trustee(s), who may be the surviving spouse, family members, or trusted third parties. The Living Trust may also provide for payment of the Grantor's debts, expenses, and taxes, if any. The Living Trust can contain the same tax and estate planning trusts and bequests as would be contained in the Grantor's will. When used, the Living Trust replaces the Will as the primary estate-planning document.

Advantages and Disadvantages of Living Trusts

A Living Trust can provide for the management of your property if you become incapable. If the Living Trust is not fully funded, you will need to also designate an agent or agents under a Durable Power of Attorney to assume that management role.

Proponents of the Living Trust place great emphasis on its effectiveness in avoiding probate. In seminars, Living Trust marketers often exaggerate the costs, complexities and time involved in the probate process. Wisconsin now has new simplified probate methods available in many cases, the option for administrative transfer of jointly-held property without probate, transfer of assets without probate through Marital Agreements, and other effective planning techniques. While Living Trusts are appropriate for some clients, other clients may benefit from these alternate methods. Although Living Trusts are uniquely effective in certain circumstances, they are not a universal estate-planning cure.

Because a Living Trust operates without court supervision, the Trustee can usually distribute Trust assets quicker than the Personal Representative of a probate estate. However, a true comparison must be made based on the nature of your assets and your unique situation. Distributions from a Living Trust may also be delayed if there are outstanding claims or taxes. With the new simplified procedures, many small estates can be transferred to heirs very quickly, without a Living Trust. Proper planning for life insurance and adequate liquid reserves can also speed up estate administration.

Because there is no court record, a Living Trust limits public disclosure of the size, contents and disposition of the Trust estate. Substantial confidentiality can also be maintained by transfers through Marital Agreements and by proper titling of assets. Although probate proceedings are matters of public record, people rarely review a probate file, unless they have a substantial personal interest.

A Living Trust will not reduce estate taxes any more than a Will. If properly drafted, both documents can include estate-planning options, including a Family Trust to permit a married couple full use of the combined Unified Credit.

A Living Trust cannot avoid all costs associated with probate. The present cost of establishing, funding and maintaining a Living Trust should be measured against the future potential savings from reduced probate fees and expenses. In some cases, these present costs may exceed the present value of projected future probate costs. Generally, Living Trusts prepared by competent estate planning attorneys, licensed in Wisconsin, are less expensive than those Living Trusts prepared by marketers.

Basic Evaluation of Living Trusts

The Living Trust is an effective and valuable method for transferring wealth and minimizing probate delays and expenses where, **after careful examination**, **it is found to be appropriate**. You must evaluate the Living Trust in light of your particular circumstances and the assets available to fund the Living Trust. You should consider, with the assistance of your advisors, all of the available methods, including Wills, Living Trusts, and Marital Agreements to transfer assets without probate, as well as the simplified administrative and probate procedures now in effect.

The Wisconsin Attorney General, various District Attorneys and other State agencies are investigating numerous consumer complaints concerning the sale of Living Trusts by individuals not licensed to practice law in the State of Wisconsin. Reputable insurance and financial planners provide a valuable service by discussing Living Trusts and other planning alternatives with their clients. However, the actual legal counseling of clients and the drafting of a Living Trust and other related documents requires legal knowledge of Wisconsin and federal taxation, elderly law, Wisconsin probate procedures, the Wisconsin Marital Property Act and other issues in which Wisconsin attorneys are educated and licensed. Licensing requirements are for your protection, as a consumer of legal services. You should be cautious of the mail order and seminar sale of Living Trusts.

Uses for Life Insurance

Most people are familiar with role of life insurance in providing cash at the time of the insured's death to satisfy anticipated needs. Because farmers' estates are often comprised substantially of assets committed to and necessary for the continuance of the farm, life insurance can be especially important in providing cash for the ongoing financial security of the surviving spouse and any dependent children, to satisfy the needs of "*on-farm*" and "*off-farm*" heirs and to pay or reduce farm debts and estate taxes.

Your life insurance plan must be based on your specific needs, including alternate sources of income, the nature and amount of your assets and debts, and your goals in transferring your farm. This planning must carefully consider the amount of insurance necessary, how policies will be owned and who will be the beneficiaries. Your estate plan must contemplate the real possibility of your premature death and the needs of your spouse, if any, and other heirs.

Who Should Own Life Insurance

Life insurance may be purchased by the insured, the insured's spouse, a child, children or other anticipated beneficiaries, or by a trust. Each ownership alternative should be considered when appropriate.

If you or your spouse own life insurance insuring either of you, you retain direct control over the policy's terms, value and beneficiary designation. However, on the insured's death, the policy proceeds will be subject to estate taxes, as part of the policy owner's estate, no matter who is the beneficiary. If the insured's spouse is the beneficiary, the policy proceeds are merely added to the spouse's estate and potentially become subject to estate taxes upon the spouse's death.

If a child, children, beneficiaries, or an Irrevocable Trust is the owner of the life insurance policy, the insured loses control of the policy but the proceeds may be excluded from the insured's estate at death.

For example, you may consider having the eventual buyer of your farm, whether a family member or a third party, own adequate life insurance on your life, so that a sale can occur at your death. As the eventual buyer is the owner and beneficiary of the policy, the proceeds are then excluded from your estate. This cross ownership of life insurance can, at least partially, finance the transfer of ownership and control to the next generation.

Irrevocable Life Insurance Trusts

If your circumstances dictate, you may consider establishing an Irrevocable Life Insurance Trust, ("*ILIT*"). The ILIT can purchase and hold as the owner and beneficiary a life insurance policy. Since you are not the owner of that policy, the death proceeds are then excluded from your estate. If the beneficiaries are your "*on-farm*" heirs, they can use the policy proceeds to purchase farm assets. If the beneficiaries are your "*off-farm*" heirs, the policy proceeds can be used to equalize their share of the estate, while on-farm heirs receive farm assets. Such ILITs are also used to provide funds for payment of debts and estate and other taxes, with insurance proceeds not reduced by estate taxes. Irrevocable Trusts which hold life insurance must be carefully drafted by an experienced attorney to comply with applicable state and federal transfer tax rules.

Strategies for Charitable Giving

Your charitable desires can be satisfied through your commitment of time and effort and through gifts to charities during your life or upon your death. Gifts to qualified charities during your life benefit from income tax deductions. Lifetime gifts also reduce estate taxes by removing the gifted asset, and its appreciation, from your estate. Bequests to qualified charities that take place upon your death are deductible for estate tax purposes.

Today, estate-planning methods have evolved which allow donors to balance their needs for ongoing income and objectives to benefit their natural heirs and charities, while obtaining tax advantages.

Charitable Remainder Trust

A Charitable Remainder Trust, ("*CRT*"), is a trust that provides specified income to a beneficiary or beneficiaries, who may include the donor, for either a specified term or until the beneficiary or beneficiaries die. After the beneficiary's income interest ceases, the remaining Trust assets are then distributed to the qualified charities. The donor receives a charitable deduction against income tax for a part of the fair market value of the donated assets, and the donated assets avoid estate tax as they are excluded from the donor's estate.

Charitable Lead Trust

A Charitable Lead Trust reverses the process of a Charitable Remainder Trust. The Trust gives the income of the assets to a qualified charity for a certain period, after which the remainder of the Trust assets pass to the named beneficiaries. Because the named beneficiaries' interests are delayed, the gift to the beneficiaries is discounted in value reducing the gift value and any resulting gift taxes. The donated assets are then excluded from the donor's estate.

Charitable Trust planning can be very beneficial in the appropriate circumstances. However, the complexities of this planning area requires the involvement of an experienced advisor.

Planning for Second Marriages

If you or your spouse has been previously married, special issues must be considered, especially if there are children from outside of your current marriage. Without a Will, Wisconsin's laws of intestacy may transfer a part of the estate to the prior children of the decedent, in an unintended amount and manner. Your estate plan must clearly state your spouse's and your intent so that disputes among family members are avoided. Usually, Marital Property Agreements are used to define which property will be maintained by each spouse as individual property and which property will be considered marital property. The Marital Property Agreement can also specifically establish the rights and interests of each spouse's children.

Avoiding estate taxes remains a primary goal, even in second marriages. Special trusts can be included in your Will or Living Trust which allow the bequest to qualify for the unlimited marital deduction against estate taxes while assuring the remaining assets of the Trust transfer to the decedent's heirs, such as his or her children, upon the surviving spouse's death.

Planning for Unmarried Couples

Unmarried couples currently face disadvantages under both Wisconsin and federal estate tax laws. First, the unlimited marital deduction from estate tax is not available to you or your partner. Neither you nor your partner will receive the automatic spousal protections in marital property, divorce or probate procedures. Without a Will or Living Trust, your partner will not receive assets under the laws of intestacy or other substantial protection within the legal system.

Therefore, your Will, Living Trust and other estate planning documents must state your specific desires and objectives for the participation and financial security of your unmarried partner.

Chapter 8

The Professional Team

The Professionals - Who they are and what they do

To plan for retirement and to put your estate in order, you will need to use a team of professionals. A professional is a person who has a particular area of expertise. A professional should give advice only in those areas in which he or she is trained or licensed. A professional should know when to defer to other professionals if the problem is outside their area of expertise. The professional should also know how their specialty fits with other specialties to solve problems. The professional should welcome the opportunity to collaborate with other experts on your teams. When giving advice, a professional should always place the interest of the client above his or her own interest.

The following is a list of professionals to consider using in the course of estate and retirement planning and a brief description of what they do.

Attorney

Attorneys are key in any retirement and estate planning process. The attorney should be involved from the beginning. Your attorney should be familiar with retirement and estate planning issues. You may want an attorney experienced in a farmer's concerns. Remember that you are planning for what happens to the farm assets you have spent your lifetime accumulating. Most likely, you will be retiring from a career you love and moving out of the home where you built that career. Those facts make retirement and estate planning unique for farmers. Your attorney will need to have all the information you have prepared in order to have a complete picture of what you hope to accomplish with your estate and retirement plan. He/she will see to it that all necessary documents are prepared, reviewed, explained to you, signed and recorded where necessary. Your attorney will show you how the documents you sign will affect decisions made on into the future. Once you have a plan developed, no documents should be signed without review by your attorney.

Accountant or Certified Public Accountant (CPA)

The accountant or CPA's role as part of the team is that of the information gatherer. As the accountant or CPA meets with the client at least once a year in connection with the preparation of the client's income tax returns, this professional is in position to have access to all the client's financial information. The accountant or CPA often will have had a long-term relationship with the client. He/she will be familiar with the client's objectives and income needs, two of the most important aspects in developing a plan for a client. Due to the relationship with the client and access to financial data the accountant or CPA can be the point person of the team of professionals.

Farm Financial Consultant / Ag Consultant

The role of the Farm Financial Consultant is to assist the farmer in doing financial analyses of the farm business. This person can assist in preparing detailed cash flow analyses, enterprise analyses, and business plans. The ag consultant needs to have knowledge of a wide variety of agricultural issues including economics, finance, government programs, markets, crop and livestock production, and other factors that impact the farm business.

Financial Planner

This individual is someone who helps you through a process of analyzing your financial needs and goals to develop the best plan for you. A financial planner will look at all aspects of your financial planning needs. Rather than just looking at your insurance needs or investment needs, a financial planner will help you with budgeting, tax planning, savings plans, investments, insurance and retirement planning. A <u>certified financial planner</u> is someone who is licensed and regulated by a board requiring specific education, experience, and examination.

Insurance Agent

The insurance agent can have an important role on the team of professionals. The role of the insurance agent is to offer the client adequate risk protection for the entire estate and the farm family. Financial losses due to catastrophic events can drastically change the client's retirement plans. Life Insurance may also serve as a vehicle for transferring the farm. While this professional is not involved annually in the operation, he or she will need to be involved when changes occur with the estate or within the farm business.

Banker / Loan Officer

The role of the banker is similar to that of the accountant. In his or her role of providing financial support for the farm, the loan officer will meet with the client on a regular basis. The loan officer will have knowledge of the client's debt and asset levels as well as income and expense information. The banker is often the first person to spot a financial opportunity or problem. This person can also be key on the team of professionals, especially where a farm transfer is involved.

Stockbroker

Stockbrokers, or registered representatives, make recommendations to customers on which securities they should buy or sell. The broker earns a commission on every transaction. Brokers are regulated through registration with the National Association of Securities Dealers, Inc. and the state agency that licenses brokers, the Department of Financial Institutions.

Who to have on your Team

Who to have on your team will depend on several factors. Each professional will need to contribute in the development of the overall plan. The team structure will depend on:

> Where you are now? What is your current financial situation? How many years until retirement?
>
> Where do you want to go? What are your goals and objectives and who can help you reach them?
>
> What alternatives do you have? Are there other directions in which to go? Are there other professionals that can help?
>
> What are your strengths and weaknesses? Maybe you feel comfortable making certain decisions without the need of a professional.
>
> Can the family and other team members agree on the need for this professional?
>
> How will you choose the professionals on your team?

The choice of team members is not always easy. As pointed out above, it can change with time and a particular need. A core team of an attorney, financial planner, accountant, insurance agent and ag lender may be all a person will ever need. Circumstances may change and other professionals may need to be used from time-to-time. Just remember that the professionals are working for you. They are selling their expertise and you have a right to expect expert advice. At the end of this chapter, you will find a checklist to assist you in choosing your professional team members.

The question of who should lead the team is also a difficult one to answer. Many people want to be in charge of their own destiny. These people will want to be in charge of putting a team together and making decisions. Others may want someone they trust to be the team leader. It could be their attorney, accountant, banker or spouse. What is important is that all people involved in the operation and planning are in agreement about who is in charge. All team members need to know their roles and know who the leader is.

How professionals work together

Deciding on which professionals should be on your team is important, but getting them to work together for you is essential. A team of professionals is like any other team. A successful team needs to have:

> Clearly defined goals

Clearly defined time-lines
Clearly defined roles
Clear communications between all members
A well-defined decision making process
Balanced participation between all members
Well-established ground rules
Awareness of the group process
Awareness of who is the Team Leader

A team that has all these traits should have no problem working together. Team dynamics, however, will dictate how often one will have to revisit these traits and refocus the team on the goal. An effective team leader will need to monitor team activities to make certain the team is working together.

Time Table

As with any activity, the sooner one starts the better the results will be. Building an estate starts with entry into the farm business. This is also when one should start planning for retirement. A complete business plan should include how one plans to start, grow, and exit the business. The team of professionals will change during the life of a business, as needs change. An example of team members at the various stages could be:

Entry Stage: In this stage, the team could include a banker, accountant, ag consultant, attorney, and insurance agent. The new farm owner's activities could involve: the development of the business plan, the job of the ag consultant or accountant; securing financing, the role of a banker; deciding on business structure, developing rental or purchase agreements, and other legal documents, the role of the attorney; and insuring the estate and its owners, the role of the insurance agent.

Growth Stage: The team at this stage might include an accountant, financial planner, stockbroker, attorney, and banker. During this stage, the farm business and estate would be building equity, perhaps growing in size, and adding new members. During this stage the farmer may want to expand the operation and/or take on a new partner. This could involve the banker, accountant, ag consultant, and attorney. The owner may want to change the structure of the business to take advantage of some tax savings. This might involve the use of an accountant and an attorney. The farmer may want to diversify his estate and invest some of the profits into stocks and bonds. This might involve the financial planner and stockbroker.

Exiting Stage: The professional team at this point of a business life might include a financial planner, an attorney, accountant, stockbroker and banker. During this stage, the farmer might be: looking for advice on the best way to exit the operation, this might involve a financial planner, an accountant, an attorney, and a banker; transfer the farm to the next generation, this could involve a banker, an attorney, a financial planner, and an accountant; and the farmer could sell his farm and invest the profits, this could involve an accountant, an attorney, financial planner, and a stockbroker.

A farm business is a dynamic entity that is impacted constantly by financial and economic factors, political policies, weather and climate, and many other factors. It is difficult to put the life cycle of farm business on particular time-line due to all the changes that can occur. The examples listed above are only examples of how changes over time will affect the composition of the team of professionals.

Finding the professionals to meet my needs

Putting together a team of professionals to assist you in the retirement and estate planning process will take time and effort. You should feel comfortable with each member of the team. Each of them should make you feel confident that you have put together the best experts you can to assist you. Here are some tips for helping you find the very best professionals to help you through the process.

Accountant

What certifications are presently held?
What is the level of agriculture experience with regard to accounting?
With regard to tax law?
How does the accountant stay current with farm tax law and accounting procedures?
How much retirement and estate planning for farmers does the accountant do?
What happens if clients are audited? Will the accountant provide records for audits, accompany client for audit or charge extra for audit representation?
What other management services are offered (i.e. investment counseling)?
Does the accountant carry business insurance?
What is the fee and billing procedure?

Attorney

Is the attorney in good standing with the State Bar of Wisconsin?
Is the attorney experienced in farm law issues?
Are business and estate planning services provided?
Will the attorney's schedule allow time to address the issue?
Can an estimate be placed on the length of time needed to address the issue?
Will there be a written fee agreement?

Farm Financial Consultant/Ag Consultant

Will the consultant develop, coordinate and meet with the advisory team?
Are services offered for business plan and feasibility study development?
What is the level of experience with agricultural and environmental regulations?
Are employee management programs offered?
What is the level of experience with particular types of operations/styles?
Are loan packaging services available?
What is the billing procedure for services?

Financial Planner

What kind of financial planning is provided?
How long has the financial planner been in business?
What kind of experience does the planner have in serving farmers?
What is the billing procedure for services?
Are follow-up or routine review processes offered?
Does the planner sell products (insurance; investments)?

Insurance Agent

Is the agent's license in good standing?
Is the agent readily available?
Does the company or companies the agent represents have a good reputation in Wisconsin?
Is a wide array of products available? (home, business, health, life, disability, long term care)
How much will the insurance cost?
Does the insurance plan fit within financial and budget goals?
Is regular review provided?

Banker/ Loan Officer

How much experience has the banker had in financial planning involving estate planning and retirement?
What services can the banker provide in the planning process?
Will there be charges for the services; if so, how will they be determined?

Stock Broker

Is the broker in good standing?
Does the broker represent a reputable firm?
Have there been any complaints against the broker/firm? If so, how resolved?
How will costs of service be calculated?
What is broker's track record in managing portfolios?
Besides trades, what other services are provided?