Section One:

Developing Your Vision for the Future

A Proposed Definition

Farm Transfer Planning. *n*. A process of decision-making that protects your land's agricultural and forest production while preserving family relationships and enhancing community development.

If you are to really tackle developing a plan for your farm's future, the above definition covers the essential bases. The concepts explored in this workbook go beyond simple estate planning, which is merely the distribution of your *stuff* when you die. Most folks do not like to think of their own death, and are often less interested in discussing it. Therefore, we prefer to use the word "transfer" (as in farm transfer, or even wealth transfer), mostly for the fact that transfer is about change in who farms, who owns land, and who manages the land. Your and your family's ability to manage this transfer during your life is what the future of your farm is ultimately about.

First, farm transfer planning is indeed a ***process***. As Dwight Eisenhower is supposed to have said, "The Plan is nothing. *Planning* is everything." What he surely meant was: things will change, but our ability to gather and evaluate information will enable us to make better decisions as we go along. Farm transfer planning embraces the same idea. It is not a passive event, and there is no one tool or silver bullet that will make it easy or make challenges go away. Indeed it is a series of transactions executed overtime within a flexible framework. There are tools that provide a good foundation and framework in which to make changes over time. It is the act of going through the process that makes the difference. Planning is hard work, but more likely produce the future you want for you, your family, and your farm.

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>
> *Dwight D. Eisenhower*

Your process supports better ***decision-making***. The process you employ to methodically gather information about what you and your family want for the farm and your own lives, what your farm is good for (ie. if you need income from it), and what you own and the extent of its value empowers you to choose among the tools available to you. Legal tools can be executed to minimize foreseeable risks and accomplish articulated goals, but as things change in life, the outcome those tools were designed to produce may no longer fit the situation. In other words, it does not end with the execution of a will, no matter how good you think that will expresses your desire at the time your lawyer writes it. If a will distribution scheme needlessly risks a farming heir's long term tenure on needed ground, the will cannot change itself. Only you have that power, and you need to have a flexible framework that will make needed changes easier to make as your and your family's lives unfold over the years.

Your decisions should ***reduce risks to productivity*** of the farm. If it is important to you and your family that your farm remain in the family and/or in production as it passes to the next generation, your decisions should allow for a smooth transition in the use and management of that land. If a family member is farming it, he or she will need to know their use of the land is a secure resource for their farm enterprises.

This planning process supports your true legacy: ***preserving your family***. How well your children get along after you are gone, and how they remember the example you (Mom and Dad) set for them is a true legacy. Keeping land in a family where the family relationships are deteriorating defeats the purpose of keeping wealth in the family, and often leads to loss of wealth. It certainly leads to stress on the farmer or manager of the land, causing them to pull back investment. Without planning, many families will find that land is a fertile field upon which to play out lifelong sibling rivalries.

Finally, how a family plans for the future use of their land depends in some measure on the ***community development*** around them. What programs and resources (such as marketing infrastructure) are available in a community ultimately depends on how many farms avail themselves of these resources. For example, local agricultural economic development initiatives, farmers markets and other regional distribution channels all depend on farmer and landowner participation. In a word, the relationship is symbiotic. Community development around agriculture depends on the aggregate of individual decisions that families make about their farms. It has been said that, in spite of the individualism we often associate with farming, no one has ever farmed alone.

Starting with What You Want

A farm owner's personal values will ultimately drive farm transfer decisions, and whether another – often younger – farmer will have the opportunity to farm the land. Therefore, the first question you should ask yourself is "What do you *want* to see happen to your farm?" This question comes before considering the situation through any lens of goals analysis, resource evaluation, or the laws that govern the transfer of wealth.

This question – *what do you want*? – like the farm transfer process itself, touches on a lot of seemingly different things that one may find important: keeping family harmony, passing on a farming tradition, retaining hard-earned wealth for heirs, and sometimes, simply not paying taxes to the government. Sometimes families find that their collective wants for the future of the farm, while not necessarily conflicting with each other, will nonetheless require modification and compromise.

To develop a vision for the future, it may be important that all family members share with you what they want to happen to the farm.

For example, you may simply *want* the farm to "stay in the family." What do you mean by this statement, and more importantly, *why* is this important to you? Often that "why" is simple family heritage. The desire to pass on the land to lineal heirs will drive many owners in their decision-making. Will it satisfy this obligation if one lineal heir gains title to the land? Or a non-lineal family member (ie. a nephew or niece)? If this is done, what wealth will be transferred to the other heirs?

There may be another value that drives your decisions: wanting your children to get along with each other after your decisions on the farm have been made, and ultimately carried through either by sale, gift or inheritance. To accomplish the desire that the farm land stay in the family, it may not be possible to divide it equally among heirs. Indeed, as noted in Section Two, *How Do You Own Your Property?,* creating ownership interests among multiple heirs may endanger the ability of any heir to effectively manage and earn income from the land. But with land as the highest value asset in most families, there are often few other assets to balance the overall estate equally among all the heirs.

When transferring farm wealth across generations, many people have a strong desire to treat heirs - particularly children - equally rather than fairly. "Equal" normally means an equal distribution of dollar value of the parents' wealth. "Fair," on the other hand, considers the totality of the circumstances in making distribution decisions where the heirs' absolute right to the wealth is modified in pursuit of certain goals (such as securing a farming heir's access to the land). "Fair" may also take into account the realistic need to make sure that the next generation can produce income from the land to support the elder generation in their later years.

To develop a vision for the future of the farm, it may be important that all family members share with you what they want to happen to the farm. Sometimes the response to such an exercise is apathy. If the apathy about the future of the farm comes from both Mom and Dad -- "You kids figure it out" -- it is probably best that the estate plan divides up the assets -- including the landholdings -- as equally as possible. Nonetheless, your goals for the farm - perhaps that it remain in production - may cause you to accept transferring the land outside the family.

The worksheet *Rating Family Values* consists of a number of statements to get you thinking about what is really important to you, and more importantly, why it is important. Each statement has a number value attached to rank importance that will provide a framework to prioritize your values. What will make tough decisions easier for family members will be openness in the process, where there will be no surprises that lead to distrust and ill-will among heirs. Your answers and comments to the questions will form the basis for shaping and sharing your decisions with the family. It will also help your advisers understand which planning tools are appropriate for you. Two additional worksheets offer an opportunity to assess your comfort level with certain decisions, and a chance for Mom and Dad to sketch their vision of retirement.

An underlying theme of this workbook is that there are no easy answers. Fortunately, there are legal tools available - such as trusts, business entities and other agreements - where access to income can be assured, along with a stake in the value of the land. Fairness will lie in how decisions balance the abilities of all heirs to access that wealth in the future. Fairness is also built into your family's understanding of the distribution decisions in your farm transfer plan.

The sooner Mom and Dad can gain common understanding of each other's views of "fair," the stronger the process will be. The potential heirs may not have an ultimate say, but it's important for them to at least know why you have made certain decisions.

Ultimately, whatever the various motivations, all heirs must recognize that these decisions have been tackled by generations before them, and now ultimately it is the title holders - Mom and/or Dad - who must decide. In the event they cannot recognize this, you may find that the best course of action is to keep your plans to yourselves.

Photo courtesy Washington State University

Managing Risk In Farm Transfer: The D's

Evaluating risks associated with keeping farmland available for production is an early step in building a plan to address and/or reduce these risks. What follows is a discussion about how accepting and planning for these risks will provide you information to consider in evaluating your risks and developing a plan to reduce these risks.

Developing a risk management plan should begin with developing family, business, and personal goals. If you have identified these goals in the worksheets section, then you can begin the process of developing a plan to reduce the risks associated with accomplishing these goals. The worksheet *Quick Risk Assessment* is a way to identify the risks that your proposed plan and/or agreement will face.

Planning to manage the D's
One key to beginning the process of planning is accepting that even the best laid plans sometimes do not work out. Therefore, even though we may be reluctant to discuss negative issues, it is critical to discuss the cons as well as the pros of any proposed distribution of the farm. While we cannot control the future or plan for every eventuality, recognizing as many risks as possible and communicating your concerns about these risks - particularly those that seem unique to your family's circumstances - to your professional advisers will be critical to help craft the best plan to achieve your goals.

One key to beginning the process of planning is accepting at the beginning that even the best laid plans sometimes do not work out.

There are many major events that can severely impact a farm family or a family business. For convenience, let us break them into those you cannot control and those that result of decisions gone wrong. Those you can't control are: death, disease and disability, and disaster. Those that can result from your decisions are divorce, disagreement, disengagement and debt. Planning a farm transfer without putting legal tools and agreements in place to manage the effects of these risks amounts to gambling with your future and your family's future.

Death
Planning for the eventual death of an owner or operator should consider how that person's passing will impact the ownership and management of the farm, specifically who will own, who will manage, and who will earn income from the farm. In many cases, the primary issue will be the difficulties imposed on a farm heir if the farm property is distributed equally to his or her siblings upon the last parent's passing.

It is important to understand that when a person dies, their assets are distributed according to their estate plan, or in the absence of one, by state law. The distribution plan may create co-ownership interests - known as Tenancy in Common - in the assets that may make them unavailable for continued use by the farm business. This can have a devastating effect on families when heirs have different ideas about what they want done with the assets. Under Washington state law, any fractional owner can request that a court divide or partition the land. If the land cannot be fairly divided and the farming heir cannot afford to purchase the other interests, it will likely be sold in its entirety outside the family. Though this may not often happen, the road co-owners must take in dividing up land by agreement may be one that helps their relationships to one another.

Landowners can manage risk with proper estate planning tools and/or business agreements to guide the distribution of assets. These include wills, which distribute property or place assets in a trust where they are managed and ultimately distributed by a trustee. Some landowners use "business entities," which can provide for the orderly transfer of assets through purchase options and terms advantageous to owners who are actively farming.

For farm businesses that depend on the earning capacity of a key operator, life insurance can provide protection for families and/or the business in the event of an "untimely" death of one of its members. Sometimes life insurance is purchased to buy out other member interests in an entity such as a limited liability company, per that entities operating agreement. For young families with higher debt and lower cash reserves, term life insurance may offer low cost alternative to whole life or other investment protection. Term policies only have value upon the death of the insured. Insurance is also commonly used to "equalize" wealth, allowing cash to go to some heirs while allowing a farming heir to inherit the land.

Disease and Disability
Farming is a dangerous occupation, and crippling accidents are common relative to other lines of work. Also, as grim as it may sound, there are many folks who express a desire that, given the choice, they would prefer to go suddenly after a full life. However, the more likely scenario is that all of us will experience a period of declining health later in our life. Sometimes diseases such as Parkinson's or Alzheimer's can deprive a landowner or business owner of the mental capacity legally required to make legal decisions.

Farm owners should always have a properly executed power of attorney in place in the event they become disabled. It is important to remember that one's last will and testament is only operable on the death of its creator; it has no effect prior to death. Therefore, everyone needs documents that will give a trusted person - often a family member - the ability to handle that person's affairs, both health care and financial. Their powers can be broad or restrictive, depending on the family circumstances.

Income protection may also be important for a farm family or business owner. Disability or income continuation insurance can provide the dollars to cover living or labor expenses during the period of disability.

Often, farmers operating together under a business entity such as a limited liability company will want to ensure that the operating agreement ensures that the operation will have the ability to purchase a disabled member's interest in the event of prolonged disability. This allows continuation in management, prevents the costs of the member's disability from affecting the assets of the entity, and directs that the purchase money will go to the family of that member.

Whatever the circumstances, farmers and landowners should be aware of how events such as disease and disability will affect their transfer decisions and have the legal infrastructure in place in which to make needed changes.

Disaster and Debt
The word "disaster" generally causes people to think of natural disasters like tornados, droughts, or floods. For these events, most farm operators carry the proper crop and casualty insurance, and in extreme cases the federal government often provides an additional safety net. However, a broader definition could include any non-weather event (or more likely a combination of events) which suddenly and severely impacts the farming operation, or weighs it down financially to the point it no longer has flexibility to operate. These might include an unpayable purchase demand in the event that a farmland owner requires immediate exit, or debt extended to the point where a bad year finally exhausts the debt-holder's flexibility to keep working with you.

Disaster can also come in the form of a claim from someone outside the family, such as an injured visitor to the farm, or an injured end user of the farm's product traced back to the farm. For any such events, depending on the type of your operation, the best risk management tool available will be the proper insurance tailored to your operation or risks associated with your land.

One key consideration for most farms is ensuring that liabilities caused by their operation do not allow claimants access to their personal and key assets, including the farmland. Without adequate legal entity protection, the claim of an outside creditor can be made on all of a farm's assets. Depending on the type of operation and the risks associated with such an operation -- including employees, processed farm products, on-farm visitors, etc. -- farm owners are advised to separate their operations from their land by creating a legal business entity to manage farm operations. When renting land, landowners should make sure a written agreement is in place so no inference can be made that there existed a partnership between the landowner and farm operator.

Divorce
While death is inevitable, divorce is a matter of probability that most do not plan for. Nevertheless, we know that many marriages end in divorce. Coupled with other risks involved in farming, the potential for a divorce cannot be ignored, considering the stressful nature -- both financial and physical -- of owning and operating a farm. Facing the possibility up front can alleviate some of the uncertainty about a diffusion of farm assets should a divorce happen.

One way to protect against the effects of divorce is to use operating and landholding entities for the farm. The governing agreement for such entities can spell out the buy-back options other owners or the company itself has in the event that one member suffers a divorce decree where a judge has awarded his or her share of the land or business to the estranged spouse. Such buy out provisions can be crafted to allow the members to purchase the interest over a period of time. Trusts can sometimes be implemented to similar effect, ensuring that beneficiaries of the trust are limited to lineal heirs of the trust's creator.

When developing a business arrangement it is important to consider how to take it apart if it is not working.

It may be possible to have a marital property agreement -- often called a "prenuptial agreement" -- limiting the rights of a spouse to certain assets in the event of divorce. Practically, this is not often done except where one side of the family has a lot of wealth to protect. If this is under consideration, such an agreement must be fair to both, particularly the spouse coming to the marriage from "outside" the family. Sometimes even with a marital property agreement, equitable distribution rules may cause the court to find the agreement inequitable or unenforceable. Therefore, the provisions of any marital property agreement should be thoroughly discussed between the parties and be reviewed by each with their own separate attorney prior to signing.

Lastly, in many farming situations, at least one spouse has an off-farm job. The disruption of a marriage will necessarily remove this income stream from the farming operation. Married couples considering purchasing a farm and starting a farm business may consider having an agreement between themselves about how the assets will be distributed in the case of divorce. This equally applies to unmarried couples who decide to purchase land assets together. This will save both parties a considerable amount of money in attorneys fees.

Disagreements and Disengagement

Major disagreements can emerge over time with multiple farm families involved in a farm business arrangement. Individuals, families and their circumstances change over time. As younger farm members get married and have children, their circumstances, values and goals may become quite different than when they entered into a joint farming operation with their parents or other unrelated persons. Older and younger generations will of course have different tolerance for risk, and can disagree over what direction the farm business should take. Disagreements over capital allocations can cause friction, and the speed at which farm assets are transferred to the younger generation can cause tension. Farm debt levels can cause difficulty; what the younger side sees as needed debt for expansion, the older side may see as a very real risk to their retirement assets. Any number of personal difficulties may develop between persons or families involved in the joint farm business.

All parties should know in advance what the financial implications will be when a future separation occurs.

At the commencement of a business arrangement, a plan should be developed for how multiple families will sever their joint farming operation. Generally a plan is needed where departing members receive only part of their investment at the time of severing the joint farming operations. When developing a business arrangement it is important to consider how to take it apart if it is not working. In other words, a plan for exit should be created at the same time as the plan for entry.

Business agreements such as operating agreements for a limited liability company can spell out the exit strategy in details that are both fair and affordable to all parties. Indeed, it should be clear enough that parties can make a sound decision to enter the business in the first place. These agreements can also dictate what steps the parties will go through in case of a disagreement. Similarly, leases can spell out how each party can end the arranged use of the land, and how differences will be settled.

Finally, risk analysis must include an acceptance of the cost of reducing those risks, including insurance and attorneys fees. Most folks are reluctant to put money out on the front end, but most analyses show how the up-front costs will pale in comparison. As a wise person once said, "Help me," is cheaper than "Fix me."