Frequently Asked Questions

QUESTION: *Why do I need to plan for my farm transfer?*

ANSWER: Farms are typically complex business entities that have very large capital asset investments. The process of moving the farm ownership to the next generation generally requires coordination with the family's estate plan. Failure to consider the entire family oftentimes is what creates a family split. Building a successful transfer plan requires consideration of issues such as taxes, liquidity, effective debt utilization, family dynamics, definition of the operating processes and relationships between the owners. Creating this documentation will enable good discussions about options and allow a transfer to occur as you planned it. Oftentimes some steps are skipped or forgotten, leading to a transfer event that is neither desired or optimal.

QUESTION: *What options do I have for transferring the family farm to my heirs so it stays in the family?*

ANSWER: 1. You can give the entire farm to the child or children who will operate it.

How will children not active in the farm feel about that result? Will they be happy with their inheritance compared to siblings that farm?

2. You can split the farm ownership between all your children.

Will they be able to work together? How will operational decisions be made? What do non-participating children expect for income, and how will they receive it?

3. You can create an "equitable split" of your family assets between all the children and put a plan in place to give children who do not farm assets other than farm properties.

There is no "right answer" for how the ownership and assets are divided. It is critical to examine the results of each alternative and see how that fits with your goals for the farm and your family.

QUESTION: *Does my distribution need to be "equal" to all my children to be "fair"?*

ANSWER: Is the value of $1 of farm assets equal to $1 of liquid assets? The average return on farm assets is under 3%* and a non-farming child would likely expect a significantly higher return on liquid assets they invest. Plus, if the non-farm child owns shares of a farm, their access to that capital for purchases or loans could be limited without a sale of the property itself. As a result of this relationship a non-farming child would often choose the smaller amount for their inheritance if it was in cash in lieu of farm ground. So "fair" does not need to be "equal."

Another component of the decision is the value the farming child brings to the operation from activities and efforts they are not fully compensated for. This is the "sweat equity discount" you may have heard about. Assume the farm child works with their parents starting at age 15 and continues to work until the parents pass their assets when the child is 55. So, 40 years of working the farm as a "non-owner." Were they really compensated fully for their work all those years that kept the farm profitable and even allowed it to grow? Oftentimes, they are not, so they are given a share of the farm "off the top" to compensate them for all those earlier efforts.

**2019 Iowa Farm Costs and Returns – Iowa State University Extension*

QUESTION: *What are the biggest obstacles to a successful farm transfer?*

ANSWER: Most people don't even know the questions to ask or where to start! Finding someone to help guide you through the process and help you examine the critical decisions and the options you have open to your farm and family is often a barrier.

Personal balance sheets for farm owners seldom include much in the way of assets beyond land, equipment and retirement accounts, if any. The lack of diversification in alternative assets, and the inability to create liquidity for non-farming children, is often the biggest obstacle to successfully transferring the family farm

In addition, estate transfer costs can oftentimes be a hurdle to the smooth transition of the farm. Managing these transition costs can be crucial to a successful result. Examples of these costs are:

- Probate Costs
- Income Taxes
- Estate Taxes

Balancing the desire to keep the farm in the family and keeping the family together when transferring the estate to the next generation is also often a hard endeavor.

QUESTION: *How can I balance the desire to keep my farm intact and my family happy after we are gone?*

ANSWER: This is often the biggest obstacle to a successful transfer of your farm. It may have taken numerous generations to build the operation you farm today, or your own work may have created most or all the assets you manage. In any event, the farm is a legacy most farmers value very highly. But our families are the thing we value the most. So, if you have children in the farm operation, and others outside the farm, how do you make sure the farm and the family hold together?

The key is to structure a plan where the farm operators can control the farm assets so they can be profitable and have a large enough asset base to pass to your grandchildren, should they desire to farm. That requires the family to examine ways to make liquidity available when the farm passes to the next generation to give to the non-farming children. If all the kids feel they were treated fairly, you will have set the stage for both a successful farm transition and the continuance of the close-knit family you created and value.

QUESTION: *When is the best time to transfer my farm to the next generation?*

ANSWER: You can gift part or all of the farm during your lifetime if you wish. That will allow the next generation to take on a greater role in managing, maintaining and growing the farm and to be paid for their efforts. But how will that affect your income during your retirement years? You need to consider your income needs as well as the potential loss of "step up in basis" tax benefits when you are deciding when to transfer your land and equipment.

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