Estate Planning for Farm Families

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This outline is designed to provide basic information about estate planning. It also contains specific information about the unique challenges and considerations of estate planning for farm families. The topics addressed in this outline include:

- What is estate planning?
- Why should I have an estate plan?
- What documents do I need?
- How do I get started with an estate plan?
- Can I avoid probate without using a trust?
- Will my estate be taxed? Will my heirs be taxed?
- What is the best way to transfer my farm?

Disclaimer: *This outline is designed to be educational and informative, but is not legal advice. The legal information contained in this outline is accurate today. However, estate planning is a constantly evolving subject, and laws are subject to change. Each person's situation is unique, and each estate planning document should be tailored to fit that unique situation.*

What is Estate Planning?

Estate planning involves different things for different people. Generally, estate planning means a deliberate, coordinated plan to manage and distribute your assets during your life and after you die. Estate planning allows you to ensure the orderly transfer of your assets and liabilities at death and that the person responsible for carrying out your plan is someone who you choose and trust. Estate planning can also minimize or eliminate estate taxes (or "death" taxes) and save heirs future income taxes.

Creating an estate plan requires you to think about many issues, including:

- What do you own, and what happens to it when you die?
- Who will pay your bills if you are ill?
- Who will care for your children?
- Who will make medical decisions and make sure your wishes are carried out?

Why Should You Have an Estate Plan?

There are many reasons why it may be important to you to have an estate plan:

- To simplify affairs for your family;
- To make sure your loved ones are provided for financially after your death;
- To avoid disputes between family members; or
- To avoid costs to your estate and your heirs, including taxes and probate fees.

What Documents Do I Need?

During your lifetime, it is important to have powers of attorney in place. In Wisconsin, there are two types of powers of attorney: (1) health care; and (2) financial. Both types allow the people you name to act on your behalf during your lifetime. Their authority ends at your death.

A **Health Care Power of Attorney** is a document that gives a person of your choosing (called an "agent") the ability to make health care decisions on your behalf. Your agent only gets authority if two doctors certify that you are unable to make medical decisions. The power of attorney may become activated for a short period of time and then terminate, for example while you are under anesthesia for surgery.

Sometimes you will hear people talk about a "living will" or an "advanced directive." The name that people call the document is less important than whether the document authorizes a person to act. Often a "living will" is only a statement of wishes about your care, but does not name an agent to act on your behalf to make medical decisions if you are unable.

A Health Care Power of Attorney allows your agent to make medical decisions, make end of life decisions and make decisions about organ donation. If you do not have a valid Health Care Power of Attorney in place and you become incapacitated, your family would need to get court authority to make medical decisions on your behalf. This court procedure is called a "guardianship of person," which requires both time and expense for your family.

The second type of power of attorney is a **Financial Power of Attorney**, also sometimes called a Durable Power of Attorney. This type of power of attorney gives a person of your choosing the ability to make financial and business decisions on your behalf. For example, your agent would be able to handle banking, paying bills, filing tax returns and managing real estate. The "durable" reference means that the authority stays in place even if you become incompetent.

Financial Powers of Attorney can be effective immediately at the time of signing or, like the Health Care Power of Attorney discussed above, be "springing" and only go into effect if you are incompetent.

Having a valid Financial Power of Attorney in place avoids your family having to obtain a "guardianship of estate" if you become incompetent. This court proceeding requires time and expense for your family.

Other documents that you may need vary based on the type of assets you own, the total value of your estate and your individual concerns and goals. One or more of the following documents may be necessary for you:

- Will
- Living Revocable Trust
- Irrevocable Trust
- Marital Property Agreement
- Buy-Sell Agreement
- Transfer on Death (TOD) Deed

How do I get Started with an Estate Plan?

Step One: Make a List of Assets.
In order to put together an orderly plan to pass your assets on after your death, you need to determine what you own, how it is titled and how much it is worth. Things to include are: real estate, bank accounts, life insurance, annuities, retirement accounts, stocks, investment accounts, savings bonds and business ownership interests. Gathering together the following documents before seeing an estate planning attorney will help with this process:

- **Real Estate Documents.** These might include deeds, land contracts, abstracts or title insurance policies. These documents include legal descriptions for your property and determine the record title holder and form of ownership.
- **Real Estate Tax Statements.** These help by summarizing all the real estate you own. They also give a cheap third-party value of the property.
- **Last Depreciation Schedule.** This will determine the tax value of the property.
- **Livestock Inventory.** A recent count of cows, bred heifers, open heifers, calves, bulls (if steers, include size).
- **Feed Inventory.** Give an estimate.
- **List of Machinery.** Include as much detail as you can and give an estimated value.

- **Aerial Photograph or Other Picture of Farm.** While not strictly necessary for an asset list, there is no substitute for getting a feel for the farm.
- **Acreage Breakdown.** Total acreage broken down by tillable, pasture, wooded, nonproductive.
- **Existing Documents.** If you have any estate planning documents in place, even if they are out-of-date, bring a copy.
- **Balance Sheet.** A Balance Sheet or other record that includes a list of liabilities.

If you have to produce a market value balance sheet for your bank each year, that alone can provide the majority of the information needed.

Step Two: Determine Your Goals.
What is most important to you? Is it avoiding probate or taxes? Do you want things to be as simple as possible? Or do you want to make sure there is some control over assets passing to children? Are you ready to start transitioning the farm to children? Or are you just concerned about planning in case of unexpected death?

As you consider these questions, keep in mind what share of your assets you want to go to the farm children versus the non-farm children. Also, think about what the monthly cash requirements are for your family.

If your goal includes transferring the family farm, the plan should keep in mind the following goals:

- Protect the parents' financial security;
- Give the transferee (usually the child) certainty;
- Avoid / minimize taxes;
- Give everyone peace of mind: allow the family to know what is going to happen, why, how, when and agree on the plan.

Step Three: Determine Your Primary Estate Plan Vehicle.
There are essentially three choices of the vehicle for your estate plan: (1) intestacy; (2) will; or (3) living revocable trust.

Intestacy is the choice you have made if you do not have a will or a trust. The intestacy laws are the default "Will" drafted by the Wisconsin legislature and contained in the Wisconsin statutes. If you have only been married once and only have children from that marriage, the intestacy laws provide that all your assets will pass to your spouse. If you do not have a spouse, all assets will pass to your children in equal shares. If you have no spouse or children, the assets will pass to more distant relatives, with the laws generally looking up, then out (parents, siblings, nieces/nephews).

The advantage of relying on the intestacy laws is that it is simple and free: you do not need to do anything during your lifetime. The disadvantages, however, include not having the ability to name a guardian for your minor children, not being able to choose the personal

representative who will handle your affairs or the default rules of intestacy do not reflect your wishes.

A **Will** is a document indicating how you want your assets distributed at your death. In a Will, you may name a guardian for your minor or special needs children. You also choose your personal representative, the person who will be responsible for inventorying your assets and distributing them after your death. A Will may also include trusts that are formed only if necessary, for instance an educational trust for your children if they have not reached an age you choose at your death or a credit shelter trust for estate tax planning.

When you use a Will as your primary estate plan document, you continue to own and manage your properties in your own name during your life. Because of this, a Will is sometimes viewed as a simpler and less expensive estate plan vehicle. You may sign a Will and not have to re-title or transfer any of your assets during your life. Another perceived advantage, depending on the circumstances, is that after your death, your local county court will oversee the inventory and transfer process, which is called probate.

Having to go through probate is a major disadvantage to using a Will for many people. The probate process takes time and costs money. All assets passing through probate are subject to a 0.2% inventory fee. Probate is especially cumbersome if you own real estate in other states, because more than one probate filing will be necessary: the primary probate in your state of residence and then ancillary probates in the other states in which you own real estate. Another disadvantage is a lack of privacy. All assets passing through probate will be listed on an inventory, which is filed in the public record.

The final option is a **Living Revocable Trust**. Creating a Living Revocable Trust means creating a separate legal entity to own and manage your assets, both during your life and after your death. During your life, you will be both the Trustee of the Trust (the person in charge of managing the assets) and the beneficiary of the Trust (the person who gets the income and other benefits of the property).

Once the Trust is created, it should be funded. This requires you to re-title your assets from your name into the name of your Trust. Accordingly, your land would no longer be owned by John Jones, it would be owned by the John Jones Revocable Trust. In case you forget to re-title any assets, a Trust plan will always include a "pour-over" Will – a Will that provides that any assets owned in your name at your death should be put into your Trust and the Trust will actually control the distribution of the assets.

Using a Trust plan allows your estate to avoid probate. Because all of your assets have been re-titled and owned by the Trust, at your death you do not own anything. Instead, a successor Trustee that you name in the Trust will step in, manage the assets and eventually distribute them to your heirs.

A successor Trustee can also step in if you become incompetent during your life. In this way, a Living Revocable Trust plan is also a good option for incapacity planning. A Trust plan also

maintains your privacy, since (provided your Trust is fully funded) no court filings will be necessary.

On the down side, because of the need to re-title and transfer assets, a Trust plan is more expensive than a Will plan at the outset. Additionally, if you have forgotten to re-title any of your assets in the name of the Trust and the value of those assets is more than $50,000, you will still have to go through probate to get those forgotten assets into the Trust, creating additional time delays and costs.

Can I Avoid Probate Without Using A Trust?

Depending on the type and amount of assets you own, in Wisconsin it is possible to avoid probate without using a revocable trust. Some assets, like life insurance or retirement accounts, pass directly to your heirs by nominating a beneficiary designation on the account. Bank accounts may also pass non-probate by adding POD (Payable on Death) or TOD (Transfer on Death) designations on the accounts. Alternatively, many assets can pass non-probate by holding them in joint tenancy. A relatively recent law in Wisconsin now allows owners of real estate to name beneficiaries on the title of real estate by using a Transfer on Death (TOD) designation. Finally, spouses can avoid probate on the first spouse's death by using a Marital Property Agreement. Wisconsin's Marital Property Law is discussed in more detail below.

Will My Estate Be Taxed? Will My Heirs Be Taxed?

There are three different taxes to consider: (1) Income; (2) Estate; and (3) Gift. (Note: This outline discusses federal tax. Wisconsin imposes its own income tax, but there is currently no separate Wisconsin tax for gifts or estates.)

Income Tax:

- Ordinary income tax ranges from 15% to 39.6% (plus a potential 3.8% net investment income tax and a 0.9% hospital insurance tax)
- Capital Gains tax (triggered by a sale of assets): 0% for taxpayers in 10% or 15% tax brackets; 15% for most taxpayers; 20% for high income (plus potential net investment income tax)

Gift Tax:

- $14,000 or less per person per year = no tax;
- $5.49 million of gifts given by one person over lifetime = no tax. (Note: The gift tax exemption is part of the $5.49 Million estate tax exemption.)

Estate Tax: After a tumultuous period beginning in 2009, Congress enacted "permanent" change to the estate tax. The tax-free amount was $5 million beginning in 2011, and automatically increases based on inflation. Accordingly, the 2012 tax free amount was $5.12 million; the 2013 amount was $5.25 million; the 2014 amount was $5.34 million; the 2015 amount was $5.43 million; and the 2016 amount is $5.45 million. The 2017 amount will be $5.49 million per individual. This is a unified credit amount, so it can be used either for lifetime gifts or for assets passing at death. The law also makes permanent the concept of "portability"

of the exemption. Because the tax-free amount is a per person figure, spouses can actually pass $10.98 million estate tax free. Credit shelter trust planning used to be necessary to assure that couples received the full credit amount, but now couples can carryover unused exemption by checking the box on the estate tax return.

Couples in Wisconsin also receive a capital gains tax advantage due to Wisconsin's **Marital Property Law**. Passed in 1986, the Marital Property Law changes the way that husbands and wives own their property so that the title to property does not necessarily equal the ownership of the property. Wisconsin presumes that property held in either spouse's name is marital property, which is owned as undivided 50% interests between the two spouses. For example, John and Mary Jones are married. The deed to their cabin lists John Jones as the owner. Wisconsin law presumes that John and Mary Jones own the cabin as marital property, and they each have an undivided 50% interest in the cabin.
Wisconsin's law means that, rather than each spouse owning one-half of the couple's "pie", the couple owns the whole "pie" together. The advantage is that, because the "pie" cannot be split, at the first spouse's death, all property owned by a couple as marital property receives a step-up in basis – even though the deceased spouse only owned a 50% interest. At the second spouse's death, the property again receives a step-up in basis.
Had John and Mary Jones lived in Minnesota, which has a different form of property law, and the deed to their cabin said "John and Mary Jones, husband and wife," they would only receive a step-up in basis on one-half of the value of the cabin at the first death: the half of the pie owned by the deceased spouse.

For spouses married before 1986, it is a good idea to clarify the classification of property under the Wisconsin Marital Property Law to assure the benefit of "double stepped-up basis" by entering into a **Marital Property Agreement**. You may choose to classify property as "survivorship marital property," assuring that all property passes to the surviving spouse without the need for probate.

What is the Best Way to Transfer My Farm?

The best strategy will depend on your individual situation. Generally, there are only three ways to transfer a farm:

1. Sell;
2. Gift; or
3. Inherit.

You may transfer assets directly, or through various entities, such as LLCs, corporations or trusts.

Each method of transfer has different advantages and disadvantages and will have a different effect on your overall objectives. Most plans involve some of each of these strategies.

Conclusion

Estate planning has many components, but need not be a complicated process. For many, the most difficult part of the estate planning process is getting started. For most, completing an estate plan gives a sense of relief that everything is "in order." Thus, coordinating your estate can be a rewarding process well worth your effort.

About the Speaker:

Bridget is an attorney and owner of Valley Crossing Law. She assists individuals and businesses with estate planning, probate and trust administration, business and farm succession and other business issues. While she works with a variety of individuals and businesses, Bridget's personal background growing up on a dairy farm in Marathon County, Wisconsin, uniquely qualifies her to assist farm families. Bridget works with farmers to transition and protect the family farm, establish estate plans for the families and assure succession of farm business entities.

Bridget is a frequent speaker on estate planning, farm and business topics and has addressed topics such as using a trust versus a will, planning for young families, business succession planning and transitioning the family farm. She visits monthly with Bob Bosold on WAXX 104.5 radio about topics of interest to farmers.

Bridget is an avid Green Bay Packers fan and enjoys spending Sunday afternoons at Lambeau Field. She also plays piano and performs with the University Community Chorus at UW-River Falls.

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