



AEDE-13-09

# What Should I Do With the Farm?

Jerry Mahan, Extension Educator  
Ohio State University Extension, Greene County

## Overview

Owning land was important enough for many of our ancestors to leave Europe and come to America. We see this today with the influx of dairy farmers from the Netherlands. Being a landowner has become a symbol of independence and for many of us a way of giving stability to our families and their future.

Deciding what to do with the family farm can be a daunting task at best. This decision may be guided by financial, legal, or emotional concerns. Many times the farm has been in the family's possession for many years and has both personal and historical significance. You may have arrived at a generation where no one in the family wants to or can farm. Finances may have changed where you need some of the capital tied up in the value of the land for various personal reasons including money to live on, pay medical bills, or meet current farm expenses. In some cases your heirs may be putting pressure on you for what they think is their "fair share."

Whatever your situation, the decision of what to do with the land lies with the owner(s). This person or persons have several alternatives. This fact sheet is designed to look at some of those alternatives including the pros and cons. Hopefully the information in this publication will help you make the best-informed decision based upon reliable information.

The information contained herein is not designed to replace information gained through dialogue with your attorney, family, tax advisor, Extension professional, or farm manager, but to supplement it. Nor does it minimize the importance of proper asset titling, an up-to-date will, living will, health care power of attorney, and durable power of attorney to help guide your wishes should you

be unable to make those decisions. A good estate plan is a necessity.

## What is important to you?

The decision of what to do with your farm may be guided by several factors and here is where you are urged to write down your goals and objectives. To help you identify these goals and objectives consider the following questions.

### *Present situation*

- Has the farm been in the family for a long time? Are you tied emotionally to the farm because you grew up there or inherited it from family? Do you live on the farm now? Are the sentimental values outweighed by the stress of continuing to own this farm?
- Is the land important to the farming operation as it relates to your children, to a friend, or to the community? How productive is the land?
- Does it contain "special" areas (natural, historic, or personal)?
- What is happening around the farm in terms of land use changes? Is development (housing, etc.) creeping up on the farm and threatening to engulf it?
- Are the buildings in good condition or will they soon need to be repaired/replaced?
- Is there importance placed on keeping the "rural or farm" atmosphere?
- Do you plan to leave the farm to your children? Without proper planning on your part, there may be a large difference in the after tax amount left to heirs of the estate.

**On and off farm heirs**—Being fair to all children is difficult but is best handled while you are alive. Heirs who have worked on the farm and increased its value may need to inherit the land to keep the farm as a viable economic business. Other children could be given cash or other assets of an equitable value.

**Future living expenses**—How concerned are you that an extended stay in the nursing home or medical expenses could cause the farm to be sold? If heirs value keeping the farm or depend on the farm business continuing for their well being, they may be more concerned about a possible extended nursing home stay or catastrophic medical expenses. How do you feel about this and if you wish to, can you or the beneficiary heirs fund the premiums for long-term insurance or upgrade medical insurance if need be?

**Financial value of the farm**—For tax purposes what is the basis of the farm? Compare the price paid when the farm was purchased versus its value today. If the farm was transferred as a gift the original “basis” or price paid for the farm, plus improvements, will follow the deed as opposed to a “stepped up basis” value determined at the death of the previous owner. The current market value of your farm can be determined through a formal appraisal by a certified farm appraiser. You can also look at adjacent land sales or the value the county auditor has in their files for your farm. It is important to determine early on if the farm will be valued for agricultural purposes or at the highest price it would bring on the open market.

Keep in mind an appraisal is just “an estimate of what a willing buyer might pay for the property.” This appraisal will be influenced by “like” sales of farms in the area, adjacent non-farm development, closeness to water and sewer lines, crop yields, road frontage, soil type, condition of buildings, existence of tile, and enrollment in United States Department of Agriculture (USDA) government programs. Other non-farm attributes of the farm like existence of a woods, pond, or other natural aspects of the farm may influence the value and determine what a willing buyer would pay. Enrollment of the farm in CAUV (Current Agriculture Use Valuation) will have an impact on taxes, as the farm owner will pay real estate taxes based upon the land’s use as a farm versus non-farm development. The land containing the buildings is normally taxed at a higher rate as compared to farmland. Enrollment in CAUV is done yearly through the county auditor’s office.

Farms enrolled in the Agricultural District Program through the county auditor’s office will also have their value impacted. Enrollment in this state program helps protect

farms from nuisance suits. It also gives some protection for farms from being assessed charges for public utilities (water, sewer, etc.) that passes through the property. Enrollment in the Agriculture District Program is done through the county auditor’s office every five years.

Other items impacting value would include radio towers, intrastate gas lines, easements or deed restrictions, electric utility lines and subsequent right of way, and underground fuel storage tanks. Depending on the future owner some of these items could be positive or negative.

**Heirs plan to sell**—If your heirs plan to sell the property, it is desirable that the property “basis” be “stepped up” as much as possible to reflect current market value. Keep in mind however that a “stepped up” basis may result in higher estate settlement costs. This “stepped up basis” normally would occur at the death of the owner. Life insurance is one source of funds to pay estate settlement costs.

In 2010 when the federal estate tax repeal is in effect, some estates in excess of \$1,300,000 may not receive a full step-up in basis in the estate.

**Transfer the land**—If your goal is to transfer the land for farming, transfer costs could be reduced by gifting. Property must actually change ownership and each child, spouse, or grandchild can be given \$13,000 (2009) worth of property each year without triggering a federal gift tax return (Form 709). The property’s original basis follows this gift, i.e. original cost plus improvements. If the property is sold, the new owner would have to pay federal capital gain on the sale price less the basis they received via the gift. The sale of a farm to children at below farm market value or financing it at below current interest rates is considered a gift under federal law.

**Gifts**—Property may also be gifted via the “applicable exclusion amount” (AEA). Each person can transfer property with a “fair market” value of up to \$1,000,000 to persons, other than their spouse, free of federal gift tax. Transfers to a spouse has unlimited restrictions. The AEA will shelter \$1,000,000 from federal estate tax and is in addition to the annual \$13,000 exclusion.

An annual gift tax return, IRS Form 709, is required for any year in which over \$13,000.00 is given to any one donee by any one donor. The tax return is due by April 15 on the year after the gift was made. No tax is due unless the \$1,000,000 AEA for gift tax purposes has been fully utilized by the donor. In addition, the spouse of the donor of the gift may sign the tax return to elect to have one-half of the gifts treated as having been made by the spouse. In this manner, the taxpayer may make use of the spouse’s annual exclusion.

Finally, if you make a larger gift to a 529 plan for college expenses, such as Ohio’s College Advantage Program, you may make an election on the gift tax return to treat the gift as being made over a five-year period. For example, if you made a \$65,000 transfer and made the election, you will be treated as making an \$13,000 annual exclusion gift for a five-year period, and you will not need to use any portion of the \$1,000,000 AEA for gift tax purposes.

Deciding what to do with your property is a daunting task at best. Taking into account your goals, income needs, family concerns, and values will necessitate utilizing input from others. This could include an attorney, accountant, Extension educators, farm managers, insurance agent, or bank trust officer to name a few.

Your estate plan will need to be updated annually as situations change.

**Personal finances**

What level of income do you need from the farm? This includes money to pay insurance on buildings, real estate taxes, and any other assessments. Are there needs for farm financial commitments? Do you want to be able to leave something for your children?

Is the farm making money? Would cash renting net more? Have you put money into the farm or have you taken living expenses as a draw from the farm? Is a son or daughter farming with you and if so, have they added to the value of the farm or taken more draw than they have added? Have they funded buildings or capital improvements? What level of retirement income do you need from the farm? What level of income can the heirs who take over the farm afford? How much faith do you have that the heirs who want to take over the farm can fund your retirement, if you feel retirement income from the farm is appropriate?

**Tax consequences**

**Capital gains**

Any sale of land will have tax consequences, which may be a major concern. Land sold outright will be charged capital gains tax based upon the difference between the price you paid for the land and improvements (the basis) and the current market price. For example, a farm purchased at \$500 per acre and sold for \$3,000 per acre would have a taxable gain of \$2,500 per acre. Assuming the land was held for at least one year, the following federal tax table and bracket can be used to figure your taxes.

<b>Federal capital gains tax table</b>	
<b>Federal income tax bracket</b>	<b>Maximum taxable rate</b>
Less than 15%	5%
Over 15%	15%

In the above example a person falling in the plus 15% ordinary income tax bracket would owe \$375 per acre in federal capital gains taxes, not including Ohio’s tax.

**Like-kind exchange**—Property may be exchanged for the same kind of property with little or no tax consequences (IRS Code Section 1031).

For an exchange to qualify as a like-kind exchange you must hold for business or investment purposes both the property you transfer and the property you receive. The basis of the property you receive will remain the same as the basis of the property that you gave up.

**Estate taxes**—These expenses are figured on the total value of the estate (net worth including the current market value of the land). Both federal and state estate taxes apply. Consult with your attorney or tax advisor on the federal and state estate taxes to be incurred upon your death. Be sure to include court costs and attorney fees.

**Easements and restrictions**

Agricultural land may have easements or deed restrictions that follow the deed and may impact potential use of the land. An easement can affect one or many of the property rights you as an owner possess. These “rights” may include the right of a utility company to repair, upgrade, or replace utility lines for water, sewer, telephone, and electricity. This easement may include a “right of way” of “x” number of feet whereby a utility company can move equipment and work on the lines without concern of damaging plants, structures, etc. Other examples include right of a neighbor to use your land for a driveway access or to install or connect drainage tile on your property.

A deed restriction is similar to an easement. It can place limitations on land. Some common ones include those that prevent unsightly activities or structures such as above-ground swimming pools, raising livestock, or mobile homes.

Although easements have been in existence for over 80 years we are now seeing more landowners choosing to place a conservation or agriculture easement on their property.

These conservation/agricultural easements written by the landowners restrict other non-conservation/agricultural uses on the land. They require the land be used only for agricultural and conservation purposes. Easements will be monitored and enforced by a land trust, township, municipality, or other governmental units as per IRS rules. A landowner may qualify for federal tax deductions by placing an agriculture/conservation easement on their land. The landowner might receive some compensation for an easement through federal state or local land preservation programs.

## Operating a farm with multiple heirs

Several opportunities exist for ownership of a farm by multiple parties.

A partnership can exist between two or more people. These partners can be “general” or “limited.” A limited partnership has one general partner and one or more limited partners.

In a general partnership all partners have equal ability to make management decisions (unless stated otherwise in the agreement). Each partner has no liability protection so their assets are at risk if the partnership cannot pay its debts.

Limited partners cannot make management decisions but do have personal liability protection. A limited partner can be thought of as an investor.

Partners have the option of selling their part of the business. A partnership is merely an extension of the individuals involved.

Corporations can be formed but require filing of articles with the Secretary of State office. Bylaws need to be created and officers elected. A corporation has legal rights, can make contracts, initiate legal actions, and own property. Corporations offer liability protection to its owners and managers. Corporations pay income tax. Additionally, any income distributed to partners is also taxed. To transfer ownership majority consent is not needed; the stock holder simply sells their stock to another individual unless limited by an agreement.

A Limited Liability Company (LLC) is a legal entity separate from its members. Similar to a corporation the LLC has the legal rights and duties of an individual. Like a corporation, papers must be filed with the Secretary of State office. Membership in an LLC can be restricted to members of the family and cannot be sold without consent of the other members.

An LLC can select the type of management it desires.

LLC members have limited liability protection. They can participate in management if they choose.

A Family Limited Partnership, or FLP, is a limited partnership in which ownership is restricted to a confined group—family members. This aspect differs from other types of partnerships and corporations where transfers of interest are unrestricted or are publicly traded. The FLP is a valuable tool for centralized management of a family business and passing limited partnership interests to the next generation.

A Family Limited Partnership is formed with a written partnership agreement. Provisions in the partnership agreement can restrict how or if partnership interests are transferred, sold, or encumbered. The FLP consists of general voting partners and limited non-voting partners. Typically, the senior generation acts as the general partners for the FLP and maintains control over partnership activities. The younger generation enters the partnership as limited partners, who hold ownership interest in the partnership but have little or no management authority. Eventually, limited partners transition to general partners.

Advantages of the FLP include:

- limiting ownership interest to family members,
- allowing for an incremental and smooth transfer from one generation to the next,
- having the ability to transfer partnership interest free of gift tax, and
- providing limited financial liability for limited partners.

An FLP must be registered with the State of Ohio. Forms are available from the Ohio Secretary of State.

## Other ways to farm

The amount of time/interest you have to manage or rent a farm is very important in determining whether you want to continue to have a part in the farming operation. There are also consequences in terms of income taxes if you are retired as to whether you are taking an active part in the farming operation or are renting it to someone.

Another option for keeping the farm is to cash rent the land. In this scenario the owner receives a rental fee on a per acre basis each year. Farmland can be share rented with the owner and farmer sharing in production expenses as well as grain sales.

The land could also be custom farmed. All aspects of planting, tilling the soil, weed control, and harvesting would be paid for on a per acre basis. All income from the farm would go to the farm owner.

Anyone entering into any of these types of agreements is encouraged to have the agreement in writing. Any agreements over one year in length should be recorded with the county recorder (rent or income figures do not

have to be included). All of these scenarios also provide for the landowner to gain any annual appreciation in land values.

OSU Extension has a land bid computer program to help assess the long-term effects of owning a farm based on inflation, income growth, interest rates, taxes, etc.

You as a farm owner may wish to hire a farm management company to fully manage the farm according to your wishes. A good source of these types of people can be found in the Ohio Society of Farm Managers and Rural Appraisers or through your local Extension office.

**Farm (sale of land) comparisons/options**

**Option A: Divide into 5-acre lots to be sold at auction**

(Maximum dollar method)

- \_\_\_\_\_ Acres in farm
- \_\_\_\_\_ Number parcels estimated
- X \_\_\_\_\_ Multiply selling price per parcel estimate
- = \_\_\_\_\_ Total gross proceeds from sale of farm estimated by multiplying
- \_\_\_\_\_ Less capital gains taxes
- \_\_\_\_\_ Less surveyor's expense
- \_\_\_\_\_ Less auctioneer's commission
- \_\_\_\_\_ Less auction advertising (ads, brochures, signs, auction site)
- \_\_\_\_\_ Less other expenses (for example, perk tests, soil analysis, test wells, legal fees, contracts, notary, penalties or real estate taxes for discontinuing CAUV or leaving an agriculture district)
- = \_\_\_\_\_ Total net proceeds from sale of farm
- ÷ \_\_\_\_\_ Divide number acres in farm
- = \_\_\_\_\_ Total net price per acre sold

**Option B: Sell farm in entirety to local farmer**

- \_\_\_\_\_ Number acres in farm
- X \_\_\_\_\_ Multiply sale price per acre
- = \_\_\_\_\_ Total gross proceeds from sale of farm
- \_\_\_\_\_ Less capital gains and taxes
- \_\_\_\_\_ Less surveyor (not always necessary)
- \_\_\_\_\_ Less legal fees, contracts, etc. (likely less than Option A)
- = \_\_\_\_\_ Total net proceeds from sale of farm
- ÷ \_\_\_\_\_ Divide number acres in farm
- = \_\_\_\_\_ Total net price per acre sold

Consider:

- Place an easement on farm to ensure new owner maintains it as a farm.
- Explore tax savings possibilities from donation of easement.
- Compare sale price of land with and without an agriculture/conservation easement.

**Option C: Variation of Option B**

Owner—Financed sale of land to local farmer with agriculture or conservation easement on property to ensure continued agricultural use and monitoring of the easement. (There may be legal costs on filing and writing an easement. The land trust may request a one-time tax deductible stewardship fee.)

- Stable, long-term possible income to owner, trust, estate, heirs, etc., but dependent on farmer's ability pay and cash flow farming operation.
- Income taxes from installment sale likely less than capital gains from Options A and B.
- Wide variety of repayment options (length, frequency fixed interest rate, balloon payment, down payment, etc.)
- Owner might have option to call note due after \_\_\_\_\_ years or purchaser might have option to pay-off after \_\_\_\_\_ years.

**Option D: Sell farm but keep a life estate**

Also dependent on farmer's ability to cash flow farming operation and pay you. In life estate, if the buyer can't pay, all value goes back to life estate holder. Estate settlement (tax) and nursing home problems with this one, especially when farm sold with life estate to family members.

**Option E: Donate farm to land trust or conservancy**

This can be done if there are no heirs or the heirs and owner are financially well off. This option can provide an income stream and tax benefits that are very attractive. Donating a farm in this manner can be done post mortem as well by the heirs even if it is not so stated in a will.

**Option F: Gifting**

Gifting to family members, farmer that rents the ground, to charities, to land trusts or conservancies, with charitable remainder trusts, outright, or scheduled gifting over the years are all possibilities.

**Option H: Limited liability company**

This combined with gifting of shares may cause a reduction in value when the estate is settled. This can be combined with heirs and possibly with tenant farmers, etc.

## Resources

### Web sites of interest

American Farmland Trust has several publications on farmland preservation and related topics, especially “Your Hand, Your Legacy.” [www.farmland.org](http://www.farmland.org)

Custom Farming an Alternative to Leasing. <http://www.extension.iastate.edu/agdm/crops/html/a3-15.html>

Financial Security in Later Life. This site was developed by USDA/CSREES. The purpose is to provide online educational programs for consumers and educators. Programs focus on saving, investing, and planning long-term care and retirement. <http://www.csrees.usda.gov/nea/economics/fsll/fsll.html>

Inflation calculator using consumer price index. <http://www.westegg.com/inflation/>

Medicare—In general, a citizen of the United States or permanent resident is eligible for Medicare at age 65. <http://www.medicare.gov/assistanceprograms/home.asp>.

The National Farm Transfer Network at 1-800-447-1895, 20 states have these programs. <http://www.extension.iastate.edu/nftn> or phone 1-800-633-4227.

Ohio Department of Aging—This web site provides information on programs and services, publications, and how to locate your local Area Agency on Aging. <http://www.goldenbuckeye.com/>

Ohio Department of Insurance. Shoppers guides for Medicare supplement insurance and long-term care insurance are on the web at <http://www.ohioinsurance.gov/consumerv/ocs/MedGuide/MedicareShoppersGuide.htm> and <http://www.ohioinsurance.gov/consumerv/ocs/LTCareGuide/LTCShoppersGuide.htm>.

Ohio Office of Farmland Preservation. <http://www.ohioagriculture.gov/farmland.stm>

Ohio Senior Health Insurance Program (OSHIP). <http://www.ohioinsurance.gov/ConsumServ/Oshiip/WhatisOSHIIP.htm>. You may also contact them by calling 1-800-686-1578 or 1-800-686-1526.

Ohio State University Extension fact sheet “Net Worth.” This worksheet helps you identify and list your assets and debts and can be downloaded from: <http://ohioline.osu.edu/mm-fact/0010.html>

Ohio State University Extension, Hocking County at [hocking.osu.edu](http://hocking.osu.edu). Web site contains Estate Planning Fact Sheet Series.

Ohio State University web site containing “Estate Planning Considerations for Ohio Families.” <http://ohioline.osu.edu/estate>

Purdue University web site designed to help farmers plan for retirement. <http://www.ces.purdue.edu/farmretirement>

Purdue University web site on “Who Will Get Grandpa’s Farm.” Contains a lot of good questions and background information on transferring a farm. <http://www2.ces.purdue.edu/farmtransfer/>

Social Security Administration—The site provides complete information about eligibility for retirement, disability, and survivor benefits. <http://www.socialsecurity.gov/>

### Books

*Farm Estate & Business Planning* by Neil Harl (15th edition).

*Passing Down the Farm* by Donald J. Jonovic & Wayne D. Messick.

*Preserving Family Lands* by Stephen J. Small.

### References for more information

Ohio State University Extension resources available from any Extension office or online at <http://ohioline.osu.edu>

- *Legal & Management Aspects of Ohio Farmland Leases* (FR-0001-01)
- *Leasing Farm Buildings & Livestock Facilities* (FR-7-02)
- *Tax Issues for Farm Rental Agreements* (FR-6-02)
- *Conservations Easements* (CDFS-1261-98)
- *Current Agricultural Use Value Assessment in Ohio* (CDFS-1267-99)
- *Agricultural Districts in Ohio* (CDFS-1268-99)
- *Tax Issues for Farm Rental Arrangements* (FR-0006-02)
- *Purchase of Development Right* (CDFS-1263-98)
- *Transferring Your Farm Business to the Next Generation* (OSU Bulletin 862)
- *Cash Farm Lease*—Sample form available from Extension offices
- *Land bid*—Computer software available through Extension for helping determine cash rent

### Other references

*Farmer’s Tax Guide*—Publication 225, Department of Treasury, Internal Revenue Service.

Special thanks to farmers Craig Corry and Dan Robinette, Tecumseh Land Trust; Don Breece, OSU Extension Assistant Director, Agriculture and Natural Resources; Peggy Kirk Hall, OSU Extension Legal Educator; and Jim Skeeles, OSU Extension Educator for reviewing this document.

## EMPOWERMENT THROUGH EDUCATION

Visit Ohio State University Extension’s web site “OhioLine” at: <http://ohioline.osu.edu>

Ohio State University Extension embraces human diversity and is committed to ensuring that all research and related educational programs are available to clientele on a nondiscriminatory basis without regard to race, color, religion, sex, age, national origin, sexual orientation, gender identity or expression, disability, or veteran status. This statement is in accordance with United States Civil Rights Laws and the USDA.

Keith L. Smith, Ph.D., Associate Vice President for Agricultural Administration and Director, Ohio State University Extension  
TDD No. 800-589-8292 (Ohio only) or 614-292-1868