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PLANNING FOR THE FUTURE OF YOUR FARM

Initial Thoughts

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Initial Thoughts

- This discussion will be in general terms
  - Your plan should be specific to you
  - The goal is to provide ideas, not a specific plan for you
  - If you already have a plan, don't worry if we discuss something not in your plan or different than your plan
- There is a plan for you
  - There are many legal strategies that can be used, you need to find the strategy(s) that work for your specific situation
  - If you don't already have an attorney, get with one that can help you with your plan
  - Part of the attorney's job is to help guide you through the plan from designing to implementing

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PLANNING FOR THE FUTURE OF YOUR FARM

General documents

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THE BASIC DOCUMENTS

These documents should be a part of every estate plan. The basic documents are typically form documents that an attorney can prepare quickly and relatively inexpensively.

1. Financial Power of Attorney
2. Health Care Power of Attorney
3. Living Will

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THE BASIC DOCUMENTS

These documents should be a part of every estate plan. The basic documents are typically form documents that an attorney can prepare quickly and relatively inexpensively.

1. Financial Power of Attorney
2. Health Care Power of Attorney
3. Living Will

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Financial Power of Attorney

- Principal and Agent
  You, the Principal, names another person, the Agent, to make financial decisions for you if you are unable to make decisions for yourself.
- Avoids Guardianship
  Without a POA, the probate court may need to appoint a guardian for you if you are incapacitated. Guardianships are burdensome.
- When Does Agent's Authority Begin?
  Agent's authority can begin only upon Principal's incapacitation or upon execution of POA. Often make authority active upon document execution because it can be difficult to have the Principal deemed incapacitated.
- Who Should Be Agent?
  Spouse and children are often best agents. Can be multiple people. Attorneys and banks can also serve but will usually charge a fee.

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Health Care Power of Attorney

- Principal and Agent
  Similar to Financial Power of Attorney. The Principal identifies the Agent to make health care decisions for them.
- Avoids Guardianship
  Without a POA, the probate court may need to appoint a guardian for you if you are incapacitated. Guardianships are burdensome.
- Authority Begins Upon Incapacitation
  Agent's authority only begins when Principal is incapacitated.
- Who Should Be Agent?
  Spouse and children are often best agents. Can be multiple people.
- Standard Form
  Hospitals, Physicians and Attorneys have developed a standard form for Ohio.

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Living Will

- End of Life Directive
  This document states your wishes to have artificial life support discontinued if permanently unconscious. Two physicians must determine permanent unconsciousness.
- Can Use Health Care Power of Attorney Instead
  A Living Will is optional. Without a Living Will, the Health Care Power of Attorney Agent will have authority to withdraw artificial life support if permanently unconscious.
- Physicians are Required to Notify
  You name those people who are to be notified before the the physicians or hospital discontinue life support.
- Standard Form
  Hospice, Hospitals, Physicians and Attorneys have developed a standard form for Ohio.

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PLANNING FOR THE FUTURE OF YOUR FARM

Avoiding Probate

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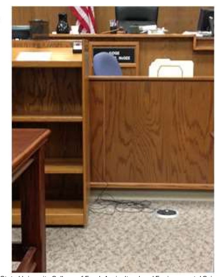
What is Probate?

- The Legal Process
  Each county has a probate court that administers certain types of property owned by someone who has died and distributes the assets to those who are entitled to receive the assets.
- Will or No Will
  If someone dies without a will or trust, their estate is intestate. The Ohio Revised Code identifies the beneficiaries of an intestate estate. Conversely, a Will or Trust identifies who is to receive the deceased person's assets. Intestacy Rules can be very different than what the deceased person would have intended.
- Probate Assets
  Assets that have been designated with a Transfer on Death or Payable on Death beneficiary are not subject to probate. Most assets can avoid probate with a beneficiary designation.



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Why Avoid Probate?

Expense
The administration of an estate can incur major expenses due to the need of a probate lawyer. Complex estates can lead to legal fees totaling in the thousands of dollars.

Time
Probate is a complex, slow process, requiring all information and documents pertaining to a decedent's assets to be presented to the court. Even with complete documentation, it can take 6-12 months, leaving heirs who wish for a quicker division of assets disappointed.

Public Information
All probate information is public. This includes the will, the assets, values and who receives which assets.

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The Process

Assets

Three different types of assets, each goes through a different process to get to beneficiaries

Beneficiaries

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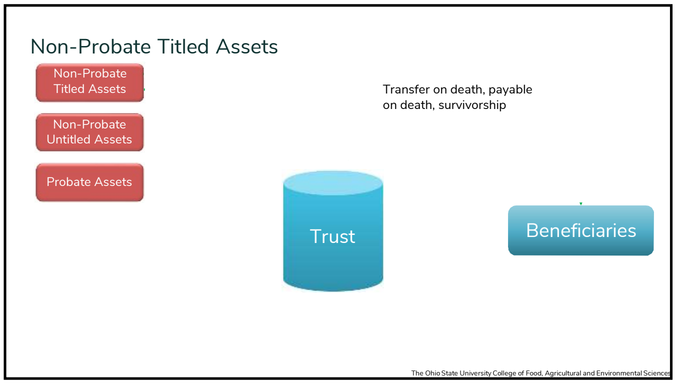
Non-Probate Titled Assets
Non-Probate Titled Assets
Non-Probate Untitled Assets
Probate Assets
Transfer on death, payable on death, survivorship
Trust
Beneficiaries
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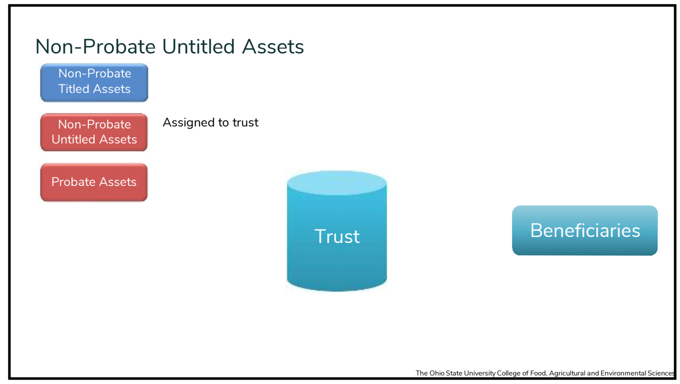
Non-Probate Untitled Assets
Non-Probate Titled Assets
Non-Probate Untitled Assets
Probate Assets
Assigned to trust
Trust
Beneficiaries
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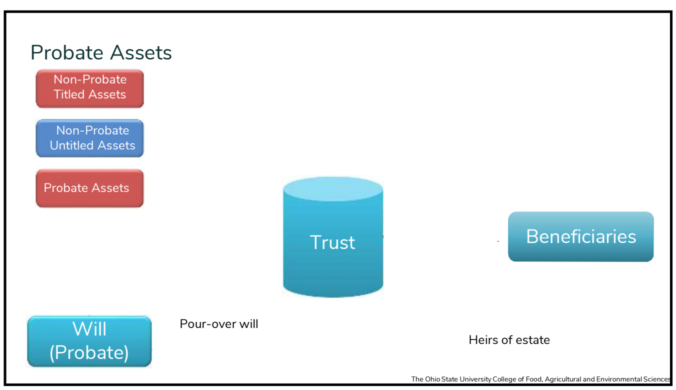
Probate Assets
Non-Probate Titled Assets
Non-Probate Untitled Assets
Probate Assets
Trust
Beneficiaries
Will (Probate)
Pour-over will
Heirs of estate
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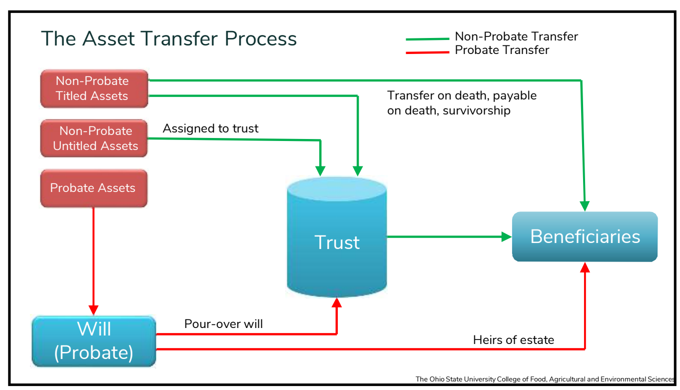
The Asset Transfer Process
Non-Probate Transfer
Probate Transfer
Non-Probate Titled Assets
Non-Probate Untitled Assets
Probate Assets
Transfer on death, payable on death, survivorship
Assigned to trust
Trust
Beneficiaries
Will (Probate)
Pour-over will
Heirs of estate
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How to Avoid Probate

Any titled asset can avoid probate.

Real Estate
All real estate can avoid probate. Joint owned land can be titled "Survivorship" and individually owned land can be titled "Transfer on Death".

Business Entities
Ownership in business entities can be made "Transfer on Death".

Bank/Financial Accounts
All bank and financial accounts can include one or more payable on death beneficiaries.

Life Insurance
Insurance policies with designated beneficiaries will avoid probate.

Retirement Accounts
Payable on death beneficiaries can be added to 401k and IRA accounts

Vehicles
A "Transfer on Death" designation can be added to any vehicle title.

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Non-Titled Assets

- What are Non-Titled Assets?
  Machinery, Livestock, Crops, Grain, Inputs
- Can Probate be Avoided?
  Yes, but only with a trust. The non-titled assets can be assigned to a trust and outside of probate.
- Should I Have a Trust to Avoid Probate?
  If the avoidance of probate is the only reason to establish a trust, it may not be sufficient to justify the cost of creating one. However, there may be other reasons that make forming a trust a worthwhile investment, even beyond avoiding probate.

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Special Rule for Surviving Spouses and Personal Vehicles

- The surviving spouse may transfer an unlimited number of vehicles valued up to $65,000 and one boat and one outboard motor without going through probate
- Only applies to personal vehicles, not trailers or commercial trucks.

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Who Does the Titling of Assets?

- Real Estate
  An attorney should draft the deed or transfer on death affidavit to title the real estate non-probate.
- Other Titled Assets
  Most other assets can have beneficiaries added or changed without the assistance of an attorney.
- Non-Titled Assets
  An attorney can prepare a simple assignment document to cause the non-titled assets to be transferred to the trust.

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Probate Costs - County Rates

Most county probate courts have established rates that probate attorneys can charge, and these fees will be approved automatically.

The county rates are a % of the value of the estate, usually 1% - 5%.

County rates may be appropriate for smaller estates and simpler estates.

Using county rates for farm estates can cause legal fees to be excessive. For example, transferring a farm valued at $1,000,000 will incur $10,000, or more, of fees using county rates.

County rates are optional, the probate attorney is not required to charge the county rates. They can charge something less or base their fees on an hourly rate. Ask the probate attorney to compare what fees will be using county rates and an hourly rate.

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Probate - Summary

Avoiding Probate

If possible and feasible, try to avoid probate since it can be slow and costly.

Titled Assets

All titled assets can be made non-probate by adding death beneficiaries. Non-titled assets can avoid probate by using a trust.

Probate Fees

Beware of county rates as the probate fees can be excessive with farm estates.

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What if You Do Not Have a Will or Trust?

- This is called intestacy
- Intestate estates are subject to probate court
- If you do not have a will or trust, Ohio law has an estate plan for you

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Intestacy Distribution

1. If no surviving spouse, to the children or their lineal descendants
2. If there is a spouse an no children, everything to spouse
3. If there is a spouse and all children are also the spouse's, everything to the spouse
4. If there is a spouse but not all children are the surviving spouse's, then divided between spouse and children
5. If no spouse and no children, everything to parents
6. If no spouse, children or parents, everything to siblings
7. If no spouse, children, parents, siblings, ½ to each set of grandparents
8. If no spouse, children, parents, siblings, grandparents, everything to next of kin
9. If no family members, everything to stepchildren
10. If no one is eligible, everything to state of Ohio

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Will or Trust?

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Will or Trust?

- Common questions is: which is better, a will or trust?
- The answer is: it depends.
- If possible, we try to get by with will because they usually incur less legal fees than a trust. However, for many farm plans, a trust is required because of complexity and succession planning issues.
- In this discussion, we will address revocable trusts, not irrevocable trusts.

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Wills and Trusts

- Transfer Assets at Death
  The primary purpose of both documents is to transfer assets to heirs and beneficiaries at death.
- Trusts
  A trust is a legal entity that can act on its own behalf through a trustee. Trusts are more flexible than wills and have several other advantages. But, trusts cost more in legal fees.
- Will
  A will is not a legal entity so the probate court has oversight and must approve the transfer of the assets
- Which Do You Need?
  Look to the different factors to determine if you need a Will or a Trust.

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Will or Trust?

Factors to Consider

	Will Plan	Trust Plan
Legal Fees		
Complexity of the plan		
Probate		
Concerns about heirs		
Surviving Spouse/ 2nd Marriage		
Transition of Farming Operation		
Estate Taxes		
Privacy		
Control		

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Legal Fees for Wills and Trusts

- Generally, legal fees will be less for wills
- Trusts are more complex documents and time must be spent titling assets to the trust to avoid probate
- A trust-based transition plan will usually cost several thousand dollars (or more) than a will-based plan.
- Ask the attorney for an estimate of legal fees before starting the process

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Complexity of Plan

- The Biggest Reason Farm Plans Often Include Trusts
  Trust plans, particularly those with on-farm and off-farm heirs often include complicated provisions to assist with transferring a farming operation to farming heirs.
- Limited by Wills
  Wills can include complex provisions but it is much harder to administer. Wills are better suited to simple estates without complex provisions.
- Trusts Allow for Creativity and Flexibility
  It is possible to be more creative when designing succession plans through the use of trusts compared to those made with wills, as almost any provision can be incorporated into a trust.

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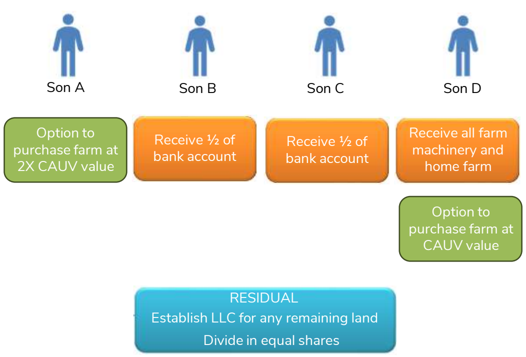

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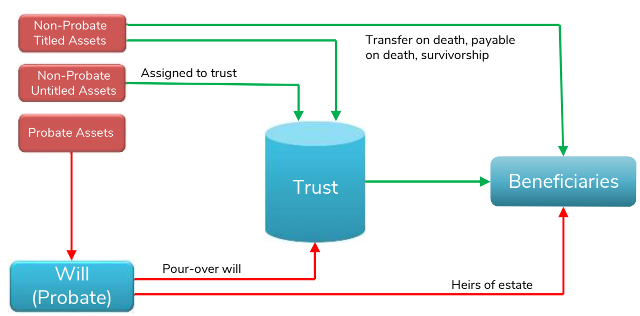
The Asset Transfer Process



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Problem Heirs/Beneficiaries

Managing Inheritance

Sometimes we have heirs or beneficiaries for whom we may have uncertainties about how they will manage their inheritance.

Many Different Issues

- Poor money managers
- Substance abuse
- Credit/financial problems
- Bad marriages

Trusts Can Help

A trust can hold the inheritance for the beneficiary, managed by the trustee, short-term or for their lives.

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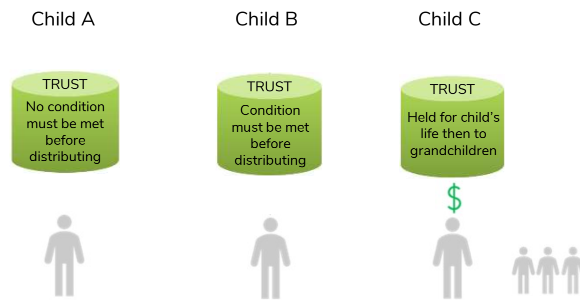
Using Trust Shares for Heirs/Beneficiaries



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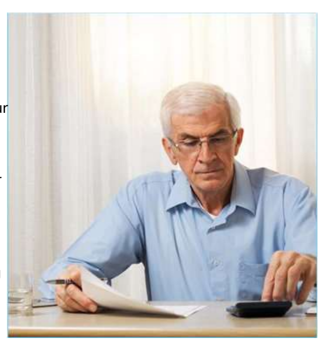
Second Spouse Marriages

- We may have concerns about leaving our assets to a second spouse
- If is possible for the surviving spouse to transfer all assets to their children rather than the deceased spouse's children/heirs
- Trusts can include plans to provide for the surviving spouse while also ensuring the deceased spouse's children/heirs inherit the property



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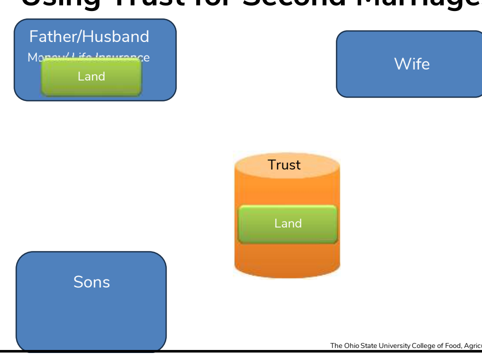
Using Trust for Second Marriages



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Transition of the Farming Operation

- Farm assets can get held up in probate
- It may take time for the executor to receive authority to act on behalf of the estate
- Examples:
  - Selling livestock and grain
  - Renewing licenses on vehicles
- Avoiding probate can allow required actions to occur faster so that the farm can be properly managed

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Estate Taxes

- Revocable trusts can help with estate taxes for married couples who will be over the federal exemption limit
- Assets of the deceased spouse can be held in their trust and the asset frozen until the death of surviving spouse
- Provides more flexibility in dealing with estate taxes
- Avoiding probate can allow required actions to occur faster so that the farm can be properly managed
- In some cases, irrevocable trusts can reduce or eliminate estate taxes

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Privacy

All probate documents are public information including the Will, assets, values and heirs

Trusts are not public documents, privacy can be protected using a trust. Only the trustee and beneficiaries are entitled to see the trust.

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Control

- We will sometimes want to retain some control over assets after death
- Wills can do this but will probably require a testamentary trust
- A trust is better at providing control
- A trust is well suited to hold assets for an extended period while certain conditions are met

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Will or Trust?
Factors to Consider

	Will Plan	Trust Plan
Legal Fees	✓	✗
Complexity of the plan	✗	✓
Probate	✗	✓
Concerns about heirs	✗	✓
Surviving Spouse/ 2nd Marriage	✗	✓
Transition of Farming Operation	✗	✓
Estate Taxes	✗	✓
Privacy	✗	✓
Control	✗	✓

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A Will or Trust?

It Depends
Whether you need a will or a trust depends on the different factors discussed earlier. This analysis should be done on a case-by-case basis.

Many Farm Plans Include Trusts
Many farm plans include trusts due to the size of the estate, complexity of plan and different types of assets.

Which is right for me?
Discus which is right for you with your attorney. Some farm transition plans can be effective only using wills.

Understanding the differences between wills and trusts can help you make an informed decision about which option is best for you.

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Irrevocable trusts

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Types of Trusts

- Revocable Trusts
  A revocable trust can be changed or terminated by the grantor during their lifetime. The assets are usually returned to the grantor upon revocation.
- Irrevocable Trusts
  An irrevocable trust cannot be changed or terminated by the grantor. The assets are transferred permanently to the trust.

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Revocable Trusts

Definition
A revocable trust can be changed or terminated by the grantor at any time. The grantor maintains control over the assets.

Control
The grantor has complete control over the assets in a revocable trust.

Flexibility
A revocable trust allows the grantor flexibility to modify the trust as their circumstances change.

Privacy
A revocable trust may provide more privacy compared to a will since it is not entered into public records upon death.

Probate Avoidance
Assets transferred to a revocable trust generally avoid probate upon the grantor's death.

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Irrevocable Trusts

Cannot Be Changed
Once an irrevocable trust is created, its terms cannot be changed by the grantor.

Cannot Be Terminated
The grantor cannot dissolve or terminate an irrevocable trust after it has been established.

Grantor Gives Up Control
By making a trust irrevocable, the grantor gives up ownership and control over the assets transferred into the trust.

May Offer Tax Benefits
Irrevocable trusts allow assets to be removed from the grantor's taxable estate, which may provide estate tax planning benefits.

May Protect Assets
An irrevocable trust may help protect assets from creditors and future beneficiaries' life events.

Requires Trustee
An irrevocable trust requires a trustee to manage the trust assets according to the trust terms.

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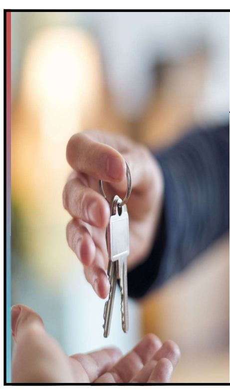

The Irrevocable Trust Strategy

Turning the keys over to your assets

- Establish an irrevocable trust and name someone else as trustee
- Transfer assets to the irrevocable trust
- Give up all ownership and control of the assets
- Because the original owner has no ownership or control of the assets, creditors cannot get to the assets
- Can be set up to not include assets in estate

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Benefits of Irrevocable Trusts

Asset Protection
Assets in an irrevocable trust are generally protected from creditors.

Tax Planning
An irrevocable trust allows for tax planning opportunities not available with a revocable trust.

Avoid Probate
Assets transferred into an irrevocable trust do not have to go through probate when the grantor dies.

Irrevocable trusts provide important benefits like avoiding probate, protecting assets, and tax planning even though the grantor gives up control.

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Disadvantages of Irrevocable Trusts

Cannot be changed after created

Once an irrevocable trust is created, its terms cannot be altered, even if circumstances change. The grantor gives up control over the assets.

May use federal estate tax exemption

Transferring assets into an irrevocable trust may be subject to gift tax if the assets exceed the lifetime gift tax exemption amount.

No flexibility

The grantor cannot access the assets in an irrevocable trust, even in an emergency. This lack of control can be problematic.

Irrevocable trusts lack flexibility but can provide some tax and asset protection benefits if structured properly.

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Gifting

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INTRODUCTION TO GIFTING STRATEGIES

Gifting strategies can be an effective way for farm families to pass on their assets to the next generation. These strategies can help to reduce the tax burden and ensure that the family's legacy is preserved. However, there are significant tax implications of gifting. Often, it is better to transfer assets through inheritance rather than gifting.

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THE ANNUAL EXCLUSION

What is the Annual Exclusion?

The Annual Exclusion is the amount of money that can be gifted to an individual without incurring a gift tax.

Who is eligible for the Annual Exclusion?

The Annual Exclusion applies to gifts made to any individual, including family members. Annual Exclusion gifts can be made to an unlimited number of people.

How much is the Annual Exclusion?

The Annual Exclusion is currently set at $17,000 per person per year.

What assets can be gifted?

Any asset can be gifted. Money, real estate, machinery, grain, livestock, business entity ownership.

Understanding the Annual Exclusion and how it applies to gifting strategies is essential for farm families looking to maximize their gifting potential.

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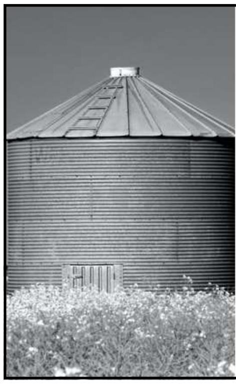

LIFETIME EXEMPTION GIFTS

Based on Federal Estate Tax Exemption
You can use your federal estate tax exemption at death, gift it during life, or a combination of both

No Gift Tax
There is no gift tax on large gifts provided a gift tax return is filed and the gift does not exceed the federal estate tax exemption.

Gift Tax Return
Must file a gift tax return if exceed annual exclusion. The gift tax return informs the IRS the size of your gift so it can be deducted from estate tax exemption.

Exemption Amount
The current exemption amount/ lifetime gift exemption is $12.9 million

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LARGE GIFT EXAMPLE

- Father gifts a farm to Daughter valued at $1,017,000.
- The first $17,000 is applied to annual exclusion.
- The remaining $1,000,000 is deducted from federal estate tax exemption.
- Father's federal estate tax exemption is reduced from $12,920,000 to $11,920,000.



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THE DOWNSIDE OF GIFTING: NEGATIVE TAX CONSEQUENCES

Gifting money or assets to family members can have serious tax implications. The biggest downside is the lost of stepped-up basis that is gained upon inheriting an asset. With everything else being equal, it is better to inherit assets than to receives assets as a gift.

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GIFTING EXAMPLE STEPPED-UP TAX BASIS

- Father owns a tractor with a FMV of $100,000 and a tax basis of $0.
- Father gifts the tractor to Daughter. Daughter receives the tractor with a $0 tax basis. Daughter has no depreciation to use.
- Instead, Father keeps the tractor and Daughter inherits. Daughter receives the tractor with a $100,000 tax basis. Daughter can re-depreciate the tractor or sell the tractor and not pay tax (if sold for $100,000 or less)
- Gifting is usually not the best tax strategy, unless avoiding estate taxes.

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TAXES AREN'T EVERYTHING: WHEN GIFTING MAKES SENSE

Avoid Estate Taxes

For people in estate tax bracket, usually better to pay capital gains than estate taxes.

Rid Yourself of Liability of Ownership

If you want to avoid the potential liability that comes with owning assets, it might be wise to transfer them now.

Timing

It may be more beneficial to give away the assets now rather than waiting for inheritance. There are numerous reasons why doing it now may be the preferable option.

Stepped-up basis at inheritance is an importance tax consideration. However, sometimes other factors justify gifting the assets and forgoing the stepped-up tax basis.

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Estate taxes

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Estate Taxes

- Ohio abolished estate taxes in 2013
- Federal estate tax exemption for 2023 is $12,920,000
- Federal estate tax exemption for 2024 is $13,610,000
- On January 1, 2026, the federal estate tax exemption is scheduled to go to $5,500,000 plus inflation
  - Probably around $7,000,000
- Congress can extend the current limit but no way to know if they will
- At present, should plan around estate taxes being $7,000,000 in 2026

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Estate Taxes

- We need to watch our net worth and any developments regarding the federal estate taxes
- If the exemption does go to $7,000,000, do not wait until the last minute to plan
- If your net worth is near or over $7,000,000, starting planning now
- Attorneys, accountants and appraisers may be very busy the last part of 2025

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PLANNING FOR THE FUTURE OF YOUR FARM

Keeping farmland in the family

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Threats to Keeping Farmland in Family

- Poor planning
- Partition
- Divorce
- Debt/Creditors
- Lawsuits

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Poor Planning

- No estate plan or a poor estate plan can jeopardize family land
- No business plan or a poor business plan can jeopardize family land
- Poor planning can cause land to be more exposed to the risks of partition, divorce, debt and lawsuits
- There are many strategies that can be implemented to help keep land in the family. Some simple, some more complex.

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Partition

- Ohio law allows a co-tenant (co-owner) of real estate to file a petition with the common please court for partition
- Partition is the process of the court selling the real estate and dividing the proceeds among the co-tenants
- Partition is the absolute right of any co-tenant although the other co-tenants have the first chance to buy the property at fair market (appraised) value
- Having multiple family members own land together invites the risk of partition

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Divorce

- Ohio law classifies assets are marital or non-marital
- Non-marital assets are not subject to divorce
- Non-marital assets
  - Assets owned prior to marriage
  - Assets inherited or received as a gift during marriage
  - Passive income and appreciation non-marital property
- Marital assets include "… all income and appreciation on separate property, due to the labor, monetary, or in-kind contribution of either or both of the spouses that occurred during the marriage."

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Multiple Strategies Available

Transfer to heirs with no restrictions or limits | Conservation/ Ag Easement | Rights of First Refusal | Long-Term Leases | LLCs | Trusts that do not allow sale of land

Spectrum of Strategies To Protect Farmland

Least Protection

Most Protection

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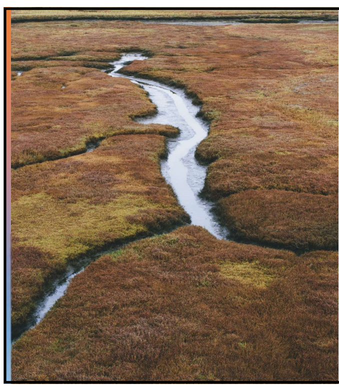

Conservation/Ag Easements

- Do not prevent transfers outside of family
- Ensures land will state undeveloped
- Help reduce value of land

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Multiple Strategies Available

Transfer to heirs with no restrictions or limits | Conservation/ Ag Easement | Rights of First Refusal | Long-Term Leases | LLCs | Trusts that do not allow sale of land

Spectrum of Strategies To Protect Farmland

Least Protection

Most Protection

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Rights of First Refusals

- Allows a family member the first right to purchase a property before it is transferred outside of the family
- If family member does not purchase, can then be transferred outside of family
- Can include favorable purchase terms

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Multiple Strategies Available

Transfer to heirs with no restrictions or limits
Conservation/ Ag Easement
Rights of First Refusal
Long-Term Leases
LLCs
Trusts that do not allow sale of land

Spectrum of Strategies To Protect Farmland

Least Protection
Most Protection

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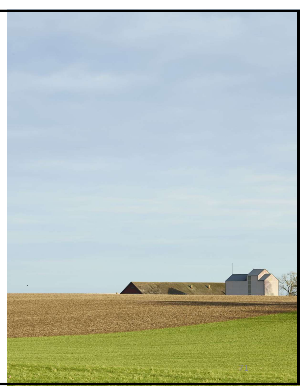
Long-Terms Leases

- Ensures that farming heir has a land base to farm
- Can be for a few years up to 99 years
- Should include a mechanism to periodically adjust lease rate
- Greatly limits what the the landowner can do with the property
  - Probably will not be able to sell the land with a long-term lease



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Multiple Strategies Available

Transfer to heirs with no restrictions or limits
Conservation/ Ag Easement
Rights of First Refusal
Long-Term Leases
LLCs
Trusts that do not allow sale of land

Spectrum of Strategies To Protect Farmland

Least Protection
Most Protection

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Limited Liability Companies (LLC)

- Eliminates partition rights
  - Partition rights only apply to real estate
- A well-designed LLC will only allow land to leave the family if the family, together, decides to transfer
- If multiple family members will own land together, consider an LLC
- Good for multiple generations to own the land together

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Multiple Strategies Available

Transfer to heirs with no restrictions or limits

Conservation/ Ag Easement

Rights of First Refusal

Long-Term Leases

LLCs

Trusts that do not allow sale of land

Spectrum of Strategies To Protect Farmland

Least Protection

Most Protection

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Trusts

- Provides the most flexibility and protection
- A trust can hold land for a beneficiary's life
  - If a beneficiary does not own the land, they cannot force the sale and their misfortunes cannot jeopardize the land
- A trust can ensure that land will not be transferred out of the family, even if the family wants to transfer
- Provides the most "from the grave" protection

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PLANNING FOR THE FUTURE OF YOUR FARM

LLCS in Farm succession – protecting farmland

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Partition Example

- Father and Mother own 600 acres
- They have three children
- They want all three children to inherit the land equally (or gift ownership to children)
- They do not want an in-law, ex-spouse, creditor, etc.... to be able to force the sale of the land
- What is the best way to accomplish the plan?

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Partition Example

Land is distributed to children as co-owners

Child A | Child B | Child C

600 Acres

Each child has partition rights

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Partition Example

Land is distributed to children as co-owners

Child A / Grandchild | Child B / Creditor | Child C / Spouse

600 Acres

Each child has partition rights

Every future owner has partition rights

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Partition Example

Land is distributed to children as co-owners

Land is distributed to children as individual owners

Child A 200 Acres | Child B 200 Acres | Child C 200 Acres

Every future owner has partition rights

Each child can sell their farm without triggering partition

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Land in the LLC

Land is put into an LLC

LLC

600 Acres

Children become co-owners of the LLC and must make decisions together

Child A Child B Child C

Creditor Spouse

3

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Land in the LLC

Land is put into an LLC

LLC

600 Acres

Even if non-family members take ownership, they have no voting rights or can be outvoted

Child A Creditor Spouse

3

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PLANNING FOR THE FUTURE OF YOUR FARM

LLCS in farm succession – non-farm heirs

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Using LLCs to Provide Assets to Off-Farm Heirs

A common challenge with farm transition planning is the need to provide for off-farm heirs but not having sufficient non-farm assets. LLCs can help overcome this issue by allowing off-farm heirs to have ownership of some farm assets.

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Challenges of Providing for Off-Farm Heirs

- Most farmers' wealth is in farm assets
- It can be problematic for the farming heir if the non-farm heirs receive farm assets.
  - The farming heir and non-farm heirs may not have same goals for assets.
  - We don't want to interfere with farming heir's ability to operate a viable farming operation.
- If non-farm heirs only receive non-farm assets, the results may not be fair or equitable.
- We often must find a way to provide at least some farm assets to the off-farm heirs for an equitable plan.
- Farming heir will still often receive more assets than non-farm heirs.

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Example: Smith Family

- Andy and Betty Smith are 60 years old and have operated a grain farming operation for 40 years
- Chris, their 30-year-old child, has been farming with them for five years and plans to take over the farming operation
- David and Elaine, their two other children, left the farm after college and have established careers off the farm.
- Andy and Betty's assets include:

$2,000,000	Land
$800,000	Machinery/Operating Assets
$200,000	Cash
$3,000,000	Total Assets

- After their deaths, Andy and Betty would like to leave about 50% of their assets to Chris and do not want to interfere with Chris' ability to operate the farm

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Example: Smith Family

Challenges for the Smith Family

- Andy and Betty want David and Elaine to receive about $750,000 each of inheritance
- There are not enough non-farm assets to satisfy the $750,000 inheritance goal
- David and Elaine will be required to receive farm assets as part of their inheritance
- David and Elaine are not active in the farming operation and we do not want their ownership of farm assets to interfere with Chris' ability to farm and make decisions.

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Andy and Betty's Estate Assets
$2,000,000 Land
$500,00 Machinery/ Op. Assets
$500,000 Cash
$3,000,000 Total

Chris
Land LLC 50% ($1,000,000)

David
$250,000 Cash
Land LLC 25% ($500,000)

Elaine
$250,000 Cash
Land LLC 25% ($500,000)

Land LLC
Chris – 50% ($1,000,000)
David – 25% ($500,000)
Elaine – 25% ($500,000)

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PLANNING FOR THE FUTURE OF YOUR FARM

LLCS in farm succession – next generation farming heir

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Using LLCs to Bring Next Generation Into Farming Operation

There are many ways to bring the next generation into the farming operation. Using LLCs or other business entities is a strategy worth exploring.

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Challenges of Bringing In Next Generation to Farming Operation

- The farming operation may have many assets and a high value
  - Farming heir may not have money to buy in
  - Parents may not want to make a large gift to transfer ownership to farming heir
- Co-owning assets with farming heir
- Gradual transfer of management/decision making
- Concerns that farming heir may not stay in farming
- Spouses, creditors, liability of farming heir

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Example: Smith Family

- Andy and Betty Smith are 60 years old and have operated a grain farming operation for 40 years
- Chris, their 30-year-old child, has been farming with them for five years and plans to take over the farming operation
- Andy and Betty own all the farm assets together which include:

$3,000,000	Land
$800,000	Machinery
$500,000	Grain
$200,000	Cash
$4,500,000	Total Farm Assets

- Andy and Betty would like to bring Chris in as a 1/3 owner of the farming operation
- Chris is newly married

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Example: Smith Family

Challenges for the Smith Family

- 1/3 of the value of all farm assets is $1,500,000
  - Chris does not have the money to buy a 1/3 interest and Andy and Betty do not want to pay tax on the sale of a 1/3 interest
  - Andy and Betty are reluctant to make a $1,500,000 gift to Chris as it would be unfair to their other children
- Andy and Betty are concerned about co-owning assets with Chris, what if they were to get divorced?
- Chris likes all the latest technology and thinks they should upgrade their machinery inventory. What if Chris spends money on something that Andy and Betty thinks they can do without?
- How do they make decisions together? Especially if they disagree on an issue?

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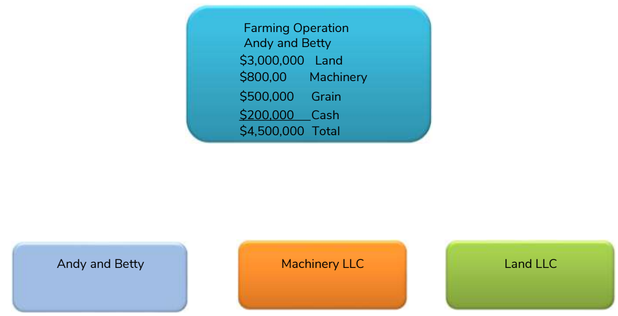

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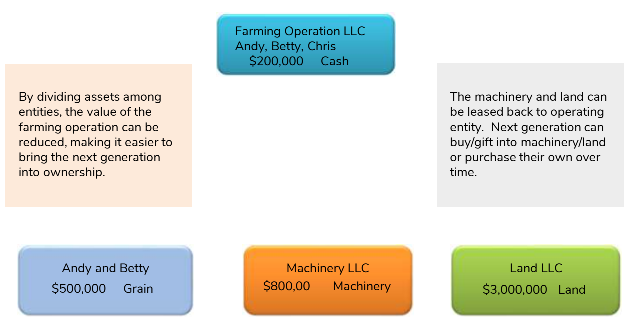

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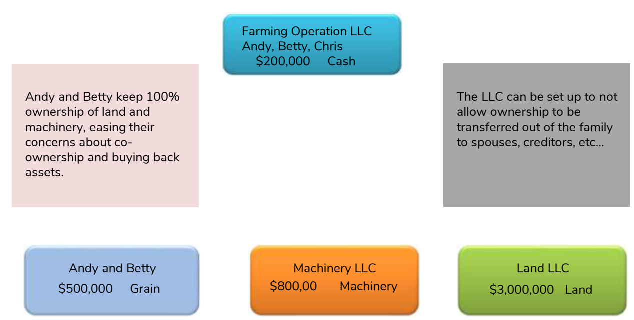

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Multiple Entity Strategy

- May not work well if the farm is already an established corporation
  - Will causes taxes if transfer assets out
- Each entity will require a bank account, accounting and tax return
- Lease payments should be made between entities to provide liability protection and legitimacy

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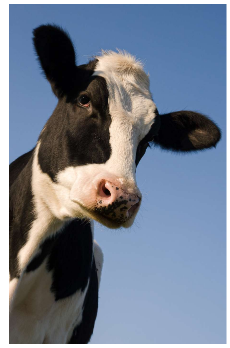

Establish New Farming Operation for Next Generation

- Sometimes it may not be feasible to bring in next generation into the current operation
  - Taxes
  - Not interested in being co-owners
- A new farming entity can be established for the next generation
- The current farming operation will subsidize with favorable lease rates, prices or other financial help
- Eventually the current farming operation transitions into an asset holding entity and does not farm

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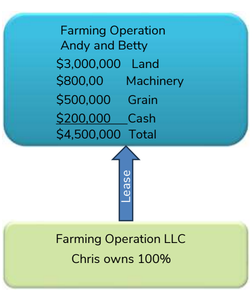

Chris leases land, machinery and buys inputs from Andy and Betty. Over time, the farming operation is transferred to Chris with Andy and Betty only owning the land.

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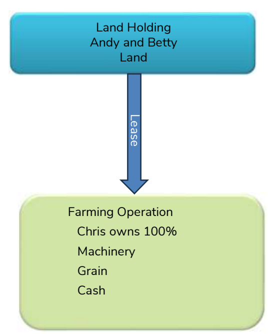

Chris leases land, machinery and buys inputs from Andy and Betty. Over time, the farming operation is transferred to Chris with Andy and Betty only owning the land. Chris' farming operation increases in size and Andy and Betty's decreases in size.

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LLCs and Transferring to the Next Generation

- Using multiple entities and new farming operating entities are two of the more common strategies to use LLC in transitioning to next generation.
- There are other strategies or combinations of strategies.
- The use of an entity(s) is not always needed or practical but should be explored when considering farm transition options.

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Long-term care

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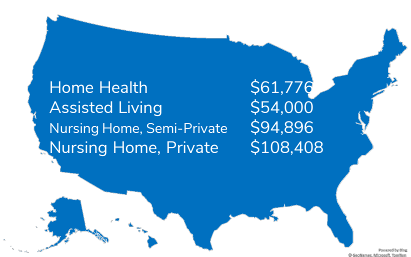
Long-Term Care Costs ($/year)

National Averages



Source: 2021 Cost of Care Survey, Genworth Financial, Inc.

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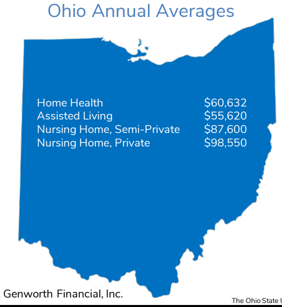
Long-Term Care Costs ($/year)

Ohio Annual Averages



Source: 2021 Cost of Care Survey, Genworth Financial, Inc.

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Long-Term Care Statistics

69% for 65

Someone turning age 65 today has a 69% chance of needing some type of long-term care services in their remaining years

Women Have Longer Lifespans

Women will need an average of 3.7 years of care and men will need 2.2 years

Some Need None, Some Need More

One-third of 65-year-olds may never need LTC, but **20% will need LTC for longer than 5 years**

Source: Administration for Community Living (acl.gov/ltc/)

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Distribution and Duration of LTC Services (69% of 65-year-olds)

3 Years of LTC	
1 year unpaid home care	$0
1 year paid home care	$61,776
1 year facility care	$94,896
Total	**$156,672**

Source: Administration for Community Living (acl.gov/ltc/)

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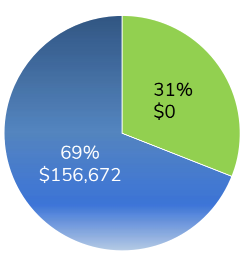
Distribution of Long-Term Care Costs



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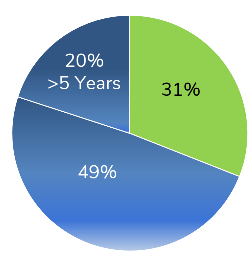
Distribution of Long-Term Care Costs



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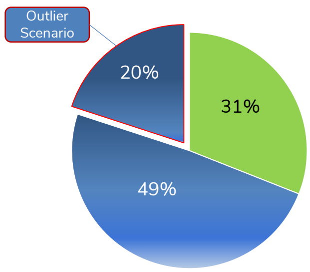
Distribution of Long-Term Care Costs



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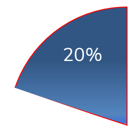
LTC Costs – Outlier Scenario



Cost of 5 years of LTC	
US	$346,464
Ohio	$323,436

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Planning Around the Outlier Scenario

- Most farms probably have enough income and savings to cover average LTC costs
- Most farms can also cover some above average costs by selling machinery, livestock and other operating assets
- Many farms' land is in jeopardy if they are an outlier
- The outlier scenario is what most farmers worry about
- We all know someone who has been in a nursing home for many years
- The average LTC scenario does not jeopardize most farms, the outlier scenario does

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The Role of Medicare

- Medicare is a federal program providing health insurance to mostly people over 65
- If the LTC costs are related to a hospital stay/skilled nursing, Medicare will pay:
  - 100% of first 20 days
  - Some portion of days 21-100
  - Nothing after day 100
- Medicare should not be included in LTC strategies

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Medicaid

- Medicaid is a joint federal and state program that provides health coverage for people with limited income and resources
- If a person does not have resources to pay for LTC, Medicaid will pay
- Medicaid eligibility is dependent upon wealth test and income test
- Few farmers will qualify for Medicaid without aggressive planning
- Medicaid has state specific rules, check your state rules

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Medicaid Asset Limits ($)

	Single	Married (both applying)	Married (one applying)
Ohio	2,000	3,000	150,620

Source: American Council on Aging

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Exempt Assets for Asset Limit Determination

- Some assets are not included in the asset limit analysis
- Rules are state specific, some assets exempt from asset limit may include:
  - Home
  - One automobile
  - Burial plot
  - Some retirement accounts
  - Property used in trade or business
- Exempt assets may still be subject to estate recovery

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Five-Year Lookback

- Assets transferred for less than FMV for the five years prior to Medicaid application are considered an improper transfer
- Improper transfer ineligibility is essentially capped at 60 months
- This rule prevents someone from giving away all their assets today and being eligible for Medicaid tomorrow
- It is a necessary rule to keep Medicaid solvent
- This rule causes LTC planning to be done five years in advance which makes LTC planning difficult and always speculatory to some degree

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Five-Year Lookback

- For each $7,453* of improper transfer, the applicant is ineligible for Medicaid for one month
  - A $100,000 gift will cause ineligibility for 14 months
  - A $1,000,000 gift will cause ineligibility for 135 months. However, by waiting 60 months to apply for Medicaid, the gift is no longer improper, and eligibility is not affected
- Timing of Medicaid application is important

*Ohio, 2023. Will vary by state and year

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The Medicaid Strategy

1. Transfer those assets to be protected by gift or other improper transfer
2. Spend down other assets, if any, to Asset Limit amount
3. Apply for and receive Medicaid to pay for LTC costs
4. Any additional assets received in the future must be spent down to regain Medicaid eligibility

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Disadvantages of The Medicaid Strategy

- May not get to select care facility
- Probably not eligible for a private room
- Receive same level of care?
- Rely on government program for care

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Long-Term Care Strategies

- Long-Term Care Insurance
- Do Nothing
- Gift Assets
- Irrevocable Trusts
- Self-Insure
- Wait and See

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Long-Term Care Insurance Strategy

- Purchase an insurance policy that will pay for at least some LTC costs
- Many types of policies and coverages
- Advantages
  - Provides protection to assets without giving up control of assets
- Disadvantages
  - Premiums can be costly, must purchase long before needed
  - Some people are not insurable
  - How much coverage to carry? How long is the term?

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Do Nothing Strategy

- For some people, adequate income is available to pay all LTC costs so no need to do anything
- For other people, must keep assets to pay expenses and/or cannot afford to transfer assets away
- The most common strategy
- Advantages
  - No cost
  - Keep full control of assets
- Disadvantages
  - No assets are protected

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Gift Assets Strategy

- Gift assets that are to be protected from LTC costs and wait for Medicaid ineligibility period to pass
- Advantages
  - Relatively inexpensive to execute
- Disadvantages
  - Loss of ownership, control and income from the assets
  - Giftee may develop their own financial issues and jeopardize the assets
  - Loss of stepped-up tax basis at death

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What Happens if Gift, Then Run Out of Money before Eligible for Medicaid?

- Gifts can be returned by giftee to avoid improper transfer status, nursing home/Medicaid cannot undo gift
- The giftees can keep the gifts and pay the LTC costs
- Giftor can apply for a hardship but must show they did everything possible to get the gifts back and no alternative income or resources are available

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Irrevocable Trust Strategy

- Transfer assets to an irrevocable trust
- Advantages
  - Trust can include an estate planning component
  - Trust can be set up to retain the income and stepped-up basis at death*
  - Can protect against giftee's financial problems and/or poor management

*Check state rules

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Irrevocable Trust Strategy

- Disadvantages
  - Can be expensive to establish and maintain trust
  - Transfer to the trusts are improper transfers, subject to five-year lookback
  - Loss of ownership and control of the assets
  - Loss of stepped-up tax basis if income or LPOA is not retained
  - Trust cannot be changed except for beneficiaries (LPOA)

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Self-Insure Strategy

- Intentionally reserve assets for LTC costs
- Usually, savings or investment accounts but can be land or other farm assets
- Advantages
  - No fees or expenses required
  - Keep full control of assets
- Disadvantages
  - How much is needed? All assets at risk if LTC costs exceed reserves
  - Impoverished spouse issue

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Wait and See Strategy

- Wait to see if LTC will be needed
- Have enough resources to pay for five years of care
- Gift assets to be protected at beginning of five-year look back period
- After five years, gifted assets are protected
- Advantages
  - Provides flexibility
  - Reduces unknown aspect of LTC planning
- Disadvantage
  - Does not protect five year's worth of assets

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Conclusion

- There are no easy solutions for LTC planning
- What is the true risk to the farm?
- Best strategy depends on risk assessment
- Each situation is different, and planning should reflect the situation

A farmer has little control over the long-term care they may need, but they do have options as to how to plan for those costs

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PLANNING FOR THE FUTURE OF YOUR FARM

Transferring farm assets

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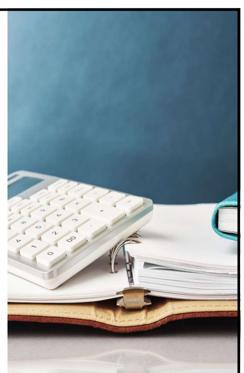
Transferring Assets During Life

- Transferring assets during life has many implications, some good some bad
- There is no perfect solution
- Each strategy has advantages and disadvantages
- Work with a tax advisor, each strategy has significant tax implications
- Gifting is not always the best strategy
- Timing is important, taxes aren't everything



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The Tax Issue

- Depreciation Recapture. Selling assets that have been depreciated will result in depreciation recapture. The recapture is treated as ordinary income.
- Capital Gains. Assets that have appreciated in value will show a capital gain when sold. Capital gains tax rates are usually lower than ordinary income rates.
- Stepped-up Tax Basis. Gifting assets does not provide a stepped-up tax basis. Inherited assets do receive a stepped-up tax basis.

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Gifting

- Transfer assets without receiving any compensation or retaining control.
- Advantages
  - Simple
  - Low cost
  - Ownership transferred immediately, relieves owner of risk
- Disadvantages
  - Owner receives no compensation
  - No stepped-up basis

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Gifting Example

- Farmer decides to retire
- Farmer does not need income from the farm machinery
- Machinery is valued at $600,000 and has $0 tax basis remaining
- Daughter is taking over farming operation and needs the machinery
- Farmer does not want to continue to own the machinery nor be responsible or liable
- Farmer gifts the machinery
- There is no tax on the gift but Daughter receives the machinery with $0 tax basis

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Outright Sale

- Sell machinery and receive one, upfront payment
- Advantages
  - Creates income
  - Ownership transferred immediately, relieves owner of risk
- Disadvantages
  - Significant tax liability
  - If selling to family, will use their resources that they could otherwise use to expand the farm

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Gradual Sale

- Sell a few items over time
- Advantages
  - Creates income
  - Spreads out income and possibly keeps in a lower tax bracket
- Disadvantages
  - Owner must wait on receiving the full amount of the sale
  - Owner retains ownership and liability of at least some of the assets

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Installment Sale

- Sell assets but receive payments over time
- Advantages
- Ownership transferred immediately, relieves owner of risk
- Disadvantages
- All depreciation recapture is due in year of sale
- Risk of not being paid
- This is usually the worst option because of the high initial taxes. The tax liability can be greater than the first year's payment.

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PLANNING FOR THE FUTURE OF YOUR FARM

Thank You!

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THE FINANCIAL POWER OF ATTORNEY

We can't always take care of our own financial and personal affairs. Whether due to medical issues, mental incapacity, schedule conflicts, or other unexpected circumstances, we sometimes need someone else to handle those needs. A Financial Power of Attorney (POA) is a legal instrument that can help in those times. It allows you as the "**principal**" to name an "**agent**" to perform duties such as managing your bank accounts, finances, and investments, signing your tax returns, or handling a specific business matter. It's a flexible legal document that you and your attorney can tailor to address different needs at different times. In this bulletin, we explain how financial POAs can be helpful to your situation and how they work.

HOW A FINANCIAL POWER OF ATTORNEY CAN HELP YOU

It gives you control. If you don't have a POA and become incapacitated, a court may have to appoint a legal guardian to act for you. The person the court selects as your guardian may be a person you wouldn't want to be involved in your affairs. With a Financial POA, you have control over who deals with your financial matters, and you can define the scope of that agent's authority.

It creates consistency. Authorizing someone to step in when you cannot avoids disruptions and keeps your finances and affairs running efficiently and smoothly.

It provides certainty. Third parties often want or require proof that someone has the legal authority to handle someone else's finances and dealings so that they don't end up in the middle of a fraud or theft situation. A Financial POA provides that proof to the parties you deal with.

THE UNIFORM POWER OF ATTORNEY ACT AND OHIO'S STATUTORY FORM

Many states, like Ohio, have adopted the **Uniform Power of Attorney Act**, a model law that provides default rules for POAs and standardizes requirements across states that adopt the law. The

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USDA United States Department of Agriculture National Agricultural Library

National Agricultural Law Center

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law aims to deter financial abuse by an "agent" appointed in a POA, especially for elderly and disabled persons. Ohio's POA Act outlines general powers of agents and includes a list of powers that a POA *does not grant* an agent unless specifically stated. These "prohibited powers" that must be stated in the POA includes power to:

- Create a trust for the principal or make changes to an existing trust
- Give away the principal's property
- Create or change rights of survivorship
- Change beneficiary designations
- Let others act in place of the named agent
- Waive the principal's right to be a beneficiary of a joint and survivor annuity, including a survivor benefit under a retirement plan.

OBTAINING, EXECUTING, AND RECORDING A POA

It is possible to prepare your own Financial POA using a state's standard form; Ohio provides an example of a POA in its statue. But you should consider **consulting an attorney** for your POA. An attorney can help you decide when you need a POA, address issues unique to your situation, help you decide what types of authority to grant an agent, and determine when the authority begins and ends. Typically, an attorney can draft a Financial POA quickly with minimal legal fees, making it well worth the investment to have a tailored document that protects you and meets your needs.

For proper execution, a person (the "principal") must sign the POA, or if unable to sign, may direct another individual to sign for the principal while in the principal's presence. Acknowledgement by a notary public or local official is the final step in the POA execution process.

If a POA is for the conveyance, mortgage, or lease of an interest in real property, it must be **recorded** in the county recorder's office where the property is located *prior to* recording of the deed, mortgage, interest, or lease. A revocation of a recorded POA must also be recorded in the same county recorder's office where the recording occurred.

GENERAL VERSUS LIMITED POAs

The two main types of Financial POAs differ according to the powers granted to the agent. A general POA grants the most authority while a limited POA limits authority to specific actions or assets.

A **general POA** typically gives the agent authority to do all things necessary to manage assets held by the principal. Examples of powers typically given by a general POA include:

- Buy, sell, lease, mortgage, and give away real and personal property.
- Contract in any manner with any person on behalf of the principal.
- Operate, buy, sell, enlarge, reduce, or terminate an ownership interest in a business.
- Open, close, invest in, and make withdrawals from an investment or bank account.
- Buy, sell, exchange, assign, settle, and exercise commodity futures contracts.
- Buy, cancel, collect, and change beneficiaries on a life insurance policy.
- Litigate for any money or other thing of value owed to the principal.
- Sign, acknowledge, seal, deliver, file, or record any instrument on behalf of the principal.
- Engage, pay, or discharge an attorney, accountant, investment manager, or other advisor.

A **limited POA** grants an agent the authority to act *only* for a specific purpose, during a certain period, or for particular assets. A limited POA will specify actions an agent may take on behalf of a principal and clarifies that the agent has no authority to act beyond that limited scope of authority. For example, a principal selling real estate might execute a limited POA that gives an agent authority to sign the deed for the principal on the day of the real estate closing. The agent does not have authority to act for the principal on any other matter or at any other time.

THE AGENT'S FIDICUARY DUTIES, LIABILITY, AND COMPENSATION

An agent has "fiduciary" responsibilities when performing under a Financial POA, which means the agent must act in accordance with the principal's best interest, in good faith, and only within the scope of the authority granted by the POA. Ohio law details the specific level of competence, care, and diligence required by an agent, as well as duties for maintaining records of receipts and disbursements and cooperating with the principal's Health Care POA to carry out health care needs, if applicable. Ohio law also states that an agent who violates the agent's duties can be financially liable for the violations. On the other hand, an agent who acts in good faith is not liable to the principal's beneficiaries or liable if the principal's property declines in value. Unless a POA states otherwise, the law states that an agent is entitled to compensation and reimbursement of expenses for performing duties, if costs are reasonable.

WHEN POA AUTHORITY STARTS AND ENDS

There are different approaches to setting the times for starting and ending a Financial POA, and it can be quite beneficial to review the options with your attorney before making decisions.

The start of POA authority. When exactly can an agent begin dealing with matters authorized by the POA? This is a very important provision of the POA to discuss with an attorney because the document will be effective immediately *unless* stated otherwise. It's typical for a principal to sign a Financial POA because the need exists at the current time, such as when a farm business owner needs an agent to assist with immediate business matters. But a second option is for a Financial POA to **"spring"** into effect only when triggered by a certain event. This type of POA can be difficult, as third parties might question whether the triggering event has occurred. For example, if a Financial POA is only effective in the event of a medical emergency, a bank might require the agent to offer proof of the medical emergency. For this reason, Ohio law allows a principal to authorize a person, such as the principal's doctor, to make a written statement that the triggering event has occurred, providing the proof necessary to confirm that the POA is valid.

Durability and incapacity. Ohio's Uniform POA Act law states that unless provided otherwise by the principal, a POA is **"durable."** This means that the Financial POA remains in effect if a principal becomes incapacitated. In the above example of a Financial POA triggered by a medical emergency, the POA would continue beyond the emergency if the principal is incapacitated by the emergency. The law provides a definition of "incapacity," which is an inability to manage property or business affairs for because a person is impaired in the ability to receive and evaluate information or make or communicate decisions, even with technological assistance, or because a person is missing, detained, or outside the United States and unable to return.

A principal may authorize someone to determine when the principal is incapacitated, or the law allows a physician or psychologist to establish incapacity and permits an attorney, judge, or government official to determine if a principal is missing, detained or unable to be in the United States.

The end of POA authority. It is also necessary to clarify when POA authority ends, or Ohio law will establish its end. If a POA states that it is not "durable," the agent's authority ends if the principal becomes incapacitated. For all POAs, the law states that an agent's authority ends if the principal dies, when the purpose of the POA is accomplished, or if the agent dies, resigns, or becomes incapacitated. A principal can change or terminate the agent's authority at any time if the principal has mental capacity. Giving notice that a POA has ended to financial institutions can ensure the agent no longer acts for the principal. Note that if the POA grants powers to convey interests in property and has been recorded, the revocation must also be recorded in the same county recorder's office.

CHOOSING AND COMMUNICATING WITH AN AGENT

Appointing someone to handle your financial and business affairs is a serious matter and exposes you to risk, regardless of how well you know the person. Choose carefully, appointing a person who will adhere to the fiduciary responsibilities the appointment requires. You can also reduce your risk by communicating the terms of the POA and your needs and wishes to your agent. Proper forethought can ensure that the POA helps you through those times when you need another to act on your behalf.

REFERENCES

Uniform Power of Attorney Act, Ohio Revised Code Sections 1337.21 to 1337.64, https://codes.ohio.gov/ohio-revised-code/chapter-1337

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PLANNING FOR THE FUTURE OF YOUR FARM

Legal tools and strategies for farm transition planning

THE HEALTH CARE POWER OF ATTORNEY AND ADVANCE DIRECTIVES

Health care decisions like deciding whether to have a medical procedure, remain on life support, or donate body organs are challenging, but what if you are incapacitated and unable to make those decisions? Or what if you have wishes for your funeral and burial that you want carried out? There are several legal documents that can address these needs. Ohio law allows you to use a Health Care Power of Attorney, Living Will Declaration, Anatomical Gifts Declaration, Donor Registration, and Statement of Funeral Arrangements to give "advance directives" about your health care and death arrangements. These are important documents that ease burdens for both you and your loved ones.

THE HEALTH CARE POWER OF ATTORNEY

A Health Care Power of Attorney (POA) is a legal document that gives the person you appoint—your "agent"—the power to determine your health care needs. Ohio law provides that, unless you express otherwise in the POA, your agent may make health care decisions to the same extent you could if you were able to do so. For example, your agent could set up appointments, choose treatment, communicate with your doctors, or decide where to obtain long term care. The Health Care POA may also include special instructions about "life support" that authorize your agent to refuse artificial or technology supplied nutrition or hydration if you are in a permanently unconscious state. Alternatively, you may have a separate Living Will Declaration that further addresses end-of-life care, discussed below. Under Ohio law, a Health Care POA begins only if your doctor determines that you have lost the "capacity" to make informed health care decisions. You may revoke or change your Health Care POA prior to death, and it extinguishes upon death.

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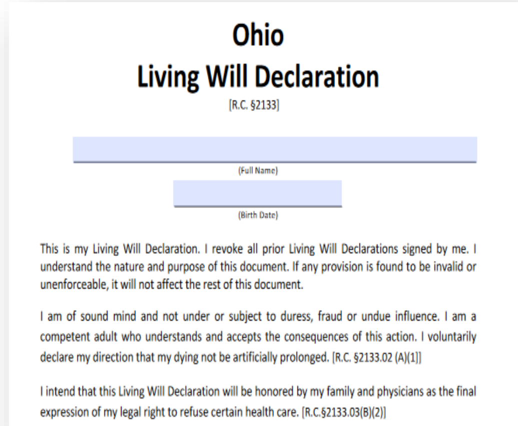
THE LIVING WILL DECLARATION

You may determine your end-of-life care through a Living Will Declaration. The declaration directs your doctor to provide only comfort and pain management care and allow you to die naturally if you are in a terminal condition or a permanently unconscious state. Your doctor is not to administer life-sustaining treatment, CPR, artificially or technologically supplied nutrition or hydration, or take any actions that postpone your death. The declaration also authorizes your doctor to issue a "Do Not Resuscitate Order."



Ohio
Living Will Declaration
[R.C. §2133]

(Full Name)

(Birth Date)

This is my Living Will Declaration. I revoke all prior Living Will Declarations signed by me. I understand the nature and purpose of this document. If any provision is found to be invalid or unenforceable, it will not affect the rest of this document.

I am of sound mind and not under or subject to duress, fraud or undue influence. I am a competent adult who understands and accepts the consequences of this action. I voluntarily declare my direction that my dying not be artificially prolonged. [R.C. §2133.02 (A)(1)]

I intend that this Living Will Declaration will be honored by my family and physicians as the final expression of my legal right to refuse certain health care. [R.C.§2133.03(B)(2)]

According to Ohio's Rights of the Terminally Ill Act, a Living Will Declaration is valid only if you are either in a terminal condition, which means an irreversible, incurable, and untreatable condition from which there is no recovery and death is likely to occur without life-sustaining equipment, or in a permanently unconscious state, which means an irreversible condition in which you are permanently unaware of yourself or your surroundings. Two doctors must examine you and agree that you are in a terminal condition or permanently unconscious state. A Living Will Declaration also directs the attending doctor to make reasonable efforts to notify at least one of three contact persons listed in the document of the determination.

ANATOMICAL GIFTS DECLARATION AND DONOR REGISTRY

Gifting body organs and tissues is also a difficult end-of-life decision to leave to your loved ones. A few options are available to make your decision known in advance and relieve stress and discord among your survivors. If you wish to make gifts of body organs and tissues, it's possible to do so in the Living Will Declaration or Health Care Power of Attorney documents explained above. Ohio and all other states also maintain a separate "donor registry system" that makes your wishes known in a medical emergency. The Ohio Bureau of Motor Vehicles oversees the registration, allowing for immediate recognition on your driver's license that you authorize donations of body organs or tissues.

DISPOSITION OF REMAINS, FUNERAL ARRANGEMENTS AND BURIAL OR CREMATION

Ohio law allows you to appoint a person who can determine what happens to your body after your death, referred to as the "right of disposition." The appointment may grant a person the right to arrange for anatomical gifts, determine the location, manner, and condition of your funeral, and make burial, cremation, and similar decisions. You may also identify the source of funds to be used to pay for arrangements. Ohio law states that a person who acts according to the appointment cannot be held liable for following your preferences. Many courts and organizations provide a form for this type of appointment.

COMMUNICATE YOUR PLANS

Let others know about your Health Care Power of Attorney and advance directives so that the documents are used if a medical or end-of-life situation arises. Give copies to those you've appointed as agents and to your doctors, attorney, and religious advisor, and keep copies with your other important records. Discuss your decisions with family and close friends. Not knowing what you would want can create stress at a very difficult time, and communicating your wishes in advance will likely reduce that stress. Even if others don't agree with your decisions, sharing them beforehand could minimize the potential of conflict, misunderstandings, or a legal battle among family members.

RESOURCES AND REFERENCES

Ohio Revised Code Chapter 1337, Power of Attorney
    https://codes.ohio.gov/ohio-revised-code/chapter-1337
Ohio Revised Code Section 2108.70, Assignment of rights regarding disposition of remains
    https://codes.ohio.gov/ohio-revised-code/section-2108.70
Ohio Revised Code Chapter 2133, Uniform Rights of the Terminally Ill Act
    https://codes.ohio.gov/ohio-revised-code/chapter-2133

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LEGAL TOOLS FOR AVOIDING PROBATE

The probate process serves the important purpose of administering a deceased person's estate. During probate, assets are accounted for, outstanding debts are paid, and property is distributed to heirs and beneficiaries, all with the oversight of the probate court. However, the probate process can be time consuming, costly, and open to public records. If these disadvantages of probate are a concern to you, note that there are other ways to distribute most your property to beneficiaries without going through probate. The law in Ohio allows you to make advance plans for transferring certain types of property outside of the probate process. In this bulletin, we begin by examining the costs of probate and then explain legal tools that allow you to avoid probate while guaranteeing that your assets transfer as you intend.

THE COSTS OF PROBATE

There can be time, privacy, and financial costs to sending farm assets through probate. In Ohio, it can take six months to a year or more for an estate to complete the probate process. Trying to continue a farm while its assets are tied up in probate for an uncertain amount of time can hinder a farming operation. Additionally, because a probate court oversees an estate going through probate, estate records are public records. Many consider this lack of privacy an additional cost of probate.

Of perhaps the most concern, however, are the financial costs for sending a farm estate through probate. The attorney that handles an estate can charge legal fees that are usually a percentage of the value of estate assets that go through probate. To limit the fees, Ohio law allows a county to set maximum probate fees attorneys can charge in the county. Even so, because farms tend to be "land rich," these legal fees can add up and amount to a significant cost. **Consider the example on the following page.**

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A county in Ohio sets the maximum fees an attorney may charge an estate in probate as:

For personal property including proceeds of real estate sold:

- 6% on the first $3,000
- 4% between $3,001 and $15,000
- 2% on the balance

For real property transferred but not sold:

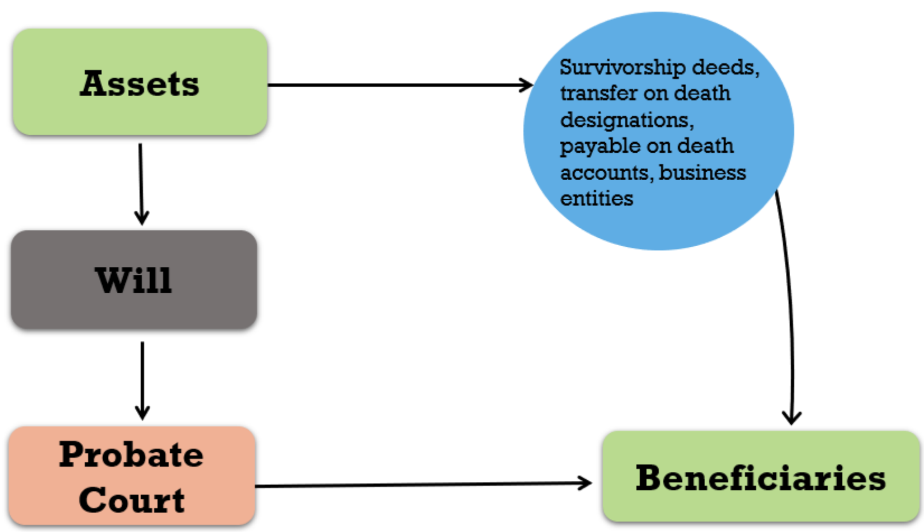
- 2% on the first $10,000
- 1% on the balance

For all other property transferred: 2% of the property value

Joe dies owning farmland valued at $500,000. The attorney could charge Joe's estate $5,100 in fees to transfer the farmland to his beneficiary.

AVOIDING PROBATE

Fortunately, there are several legal tools that can keep a farm parcel like Joe's and many other farm assets out of probate, reducing not just the financial costs but also the time and privacy costs of transferring assets through the probate process. Survivorship deeds, transfer on death designations, payable on death accounts, trusts, and business entities are the most common of these tools. We discuss trusts in another bulletin in the *Planning for the Future of Your Farm* series. The other tools, explained below, send assets directly to the intended beneficiaries rather than transferring through the estate administration process in probate court. The illustration below shows how the tools can keep assets out of probate court.



SURVIVORSHIP DEEDS

Ohio law allows co-owners of real property to pass their share of the property to the surviving co-owner(s) upon death through a survivorship deed, also referred to as a "joint tenancy with survivorship rights." This type of deed is common in a marital situation, where the spouses own equal shares in the property and each becomes the sole owner if the other spouse passes away first.

A survivorship deed is useful for other joint ownership situations in addition to marriage, whenever the owners want to ensure that their share goes only to the other co-owners upon death.

The process for establishing a survivorship deed is simple. The property deed must contain language expressing the intent of the joint owners to have survivorship rights. The language signals that the property is to transfer automatically upon death of a co-owner, making it unnecessary for the property to go through probate to accomplish a transfer of ownership. **Consider this example:**

> John and Jane are married and own farmland. The deed to the farmland states "to John and Jane Doe for their joint lives, remainder to the survivor of them." This language indicates an intent for the property to pass to the surviving spouse if the other spouse dies. Upon John's death, the property automatically vests with Jane, who becomes the sole owner of the property. The property does not have to go through the probate process to transfer to Jane.

TRANSFER ON DEATH AFFIDAVIT

Another instrument for designating a transfer of real property upon an owner's death is the "transfer on death designation affidavit." This affidavit allows property to pass to one or more designated beneficiaries if the owner dies. The process is simple but requires a few forms and steps. First, the owner must complete the affidavit and file it with the recorder in the county where the land is located. Then, upon the owner's death, the designated beneficiary must complete an affidavit of confirmation and present it to the county auditor and county recorder along with a verified death certificate for the deceased owner. Once the county recorder files the affidavit of confirmation, the beneficiary holds title to the deceased owner's share of the designated property.

TRANSFER ON DEATH DESIGNATION AFFIDAVIT
[RC 5302.22]

STATE of OHIO
COUNTY of ______________

____, owner, with a marital status of__________________, now owner of record of the following real property located at ____ as recorded at Instrument No. ____________________________of __________ County deed records, with the following legal description:

Title of record to the above property is held by owner(s) as follows:
____ Sole owner
____ Tenant(s) in common
____ Tenant(s) in survivorship
____ Tenant(s) by the entireties

Hereby designates the following as transfer on death beneficiary to receive the owner's title to that property upon the death of the owner:
____.

VEHICLES

Ohio law also allows motor vehicles, boat, campers, and mobile homes to transfer outside of probate with a transfer on death designation made by completing and filing a Transfer on Death Beneficiary Designation (form BMV 3811) at the county clerk of courts title office. The beneficiary may be an individual, corporation, organization, trust, or other legal entity.

There is a special rule for automobiles owned by a deceased spouse that did not include a transfer on death designation. Upon the death of a married person who owned at least one automobile at the time of death, the surviving spouse may transfer an unlimited number of vehicles valued up to $65,000 and one boat and one outboard motor by taking a death certificate to the title office and completing a Surviving Spouse Affidavit (form BMV 3773). It is important to note that the deceased spouse provision only applies to automobiles used "as a method of conveyance." Grain trucks, trailers and other commercial vehicles are typically not permitted to transfer using this method.

PAYABLE ON DEATH ACCOUNTS

Farmers may have several other types of accounts that can pass automatically to identified beneficiaries. Checking accounts, savings accounts, stocks and bonds, IRAs, life insurance policies, and similar types of accounts can pass outside of probate if designated by the owner as "payable on death." The institution that holds the account requires an owner to complete the institution's forms to make a payable on death designation. As with transfer on death affidavits, the institution will require the named beneficiary to provide a certified copy of the owner's death certificate before transferring the account to the named beneficiary, and the account need not go through the probate process. Institutions often ask for beneficiary designations when a person opens an account, but owners may forget about these designations or fail to change them as circumstances change. For these reasons, it is good practice to review and update your payable on death designations regularly.

BUSINESS ENTITIES

The many advantages of using business entities are well known but avoiding probate is an often-overlooked attribute of business entities. Ohio law allows business entity ownership to be transferred outside of probate by making a transfer on death designation. This is most commonly done with ownership certificates or within the operating agreement. Upon the death of the owner, the ownership is transferred to the designated beneficiary with a simple transfer business document.
Consider the following example:

> Andy and Betty own XYZ Farms LLC. Andy wishes for his ownership to transfer to Betty upon his death. To avoid probate, Andy and Betty create ownership certificates for the LLC. Andy's certificate is titled "Andy, transfer on death, to Betty". This simple certificate with this simple phrase causes Andy's ownership to pass to Betty outside of probate.

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Business entity ownership certificates can be relatively simple and are often drafted by the attorney setting up the entity. The certificates do not need to be recorded; they remain private business documents. Existing entities without certificates can create new certificates for a transfer on death designations. Upon establishing a new entity, certificates should be drafted to allow for a transfer on death designation.

NON-TITLED ASSETS

As the above discussion shows, Ohio law allows titled assets to avoid probate rather easily. However, farms have many untitled assets such as machinery, equipment, livestock, crops, and grain. These assets can be made non-probate, but it will require either a trust or a business entity.

The non-titled assets can be transferred to a trust then distributed to beneficiaries without the need of probate. In a similar manner, non-titled assets can be transferred into a business entity and the entity ownership certificates made to include a transfer on death designation. If neither a trust nor business entity is used, the non-titled assets will likely need to pass through probate upon the death of the owner.

REVIEWING YOUR NON-PROBATE TRANSFER OPTIONS

It's surprising to learn how much of an estate can transfer to beneficiaries without going through the probate process. Whether you need a simple or complex transition and estate plan, these tools will likely contribute to your plan. Review your assets and their transfer options with your attorney to see how these tools can help you plan for the future of your farm.

REFERENCES

Ohio Revised Code Section 5302.20, Survivorship tenancy
https://codes.ohio.gov/ohio-revised-code/section-5302.20
Ohio Revised Code Section 5302.22, Transfer on death deed form
https://codes.ohio.gov/ohio-revised-code/section-5302.22
Ohio Revised Code Section 2106.18, Transfer of vehicle by surviving spouse
https://codes.ohio.gov/ohio-revised-code/section-2106.18
Ohio Revised Code Section 2106.18, Transfer on death designation for business entities
https://codes.ohio.gov/ohio-revised-code/section-1709.05

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GIFTING ASSETS PRIOR TO DEATH

Gifting assets before your death may seem like an obvious strategy for those who want to transfer assets to their heirs. If you don't need the assets, why not transfer them now rather than after your death? It's true that gifting can be a good strategy for transferring assets, but gifting can have tax implications and transferring the same assets through an estate plan may be a better strategy. In this bulletin, we discuss how gifting works, gifts and taxes, and when it is advantageous to incorporate gifting into a farm transition plan.

WHAT IS A GIFT?

According to the Internal Revenue Service (IRS), a gift is property transferred to another without receiving the full value of the property in return. Just about any asset can be a gift. Cash is the most common gift but many farm families also gift machinery, livestock, grain, and land.

MAKING A GIFT

The process for making a gift depends upon the asset being gifted. Some assets can only be gifted by executing documents while other assets can be gifted by simply handing the asset over to the person receiving the gift. Here is a list of commonly gifted assets and how they are gifted:

- **Real estate.** May only be transferred with properly executed deeds.
- **Financial accounts**. Transfer forms must be completed with the financial institution.
- **Vehicles and trailers.** Title must be transferred, and a new title issued by the county Clerk of Courts title office. Note that some smaller trailers may not have titles.
- **Machinery, equipment, livestock, and grain**. These assets do not have titles, so they are transferred by giving possession of the asset to the giftee.
- **Cash.** Direct transfer of funds to the giftee.

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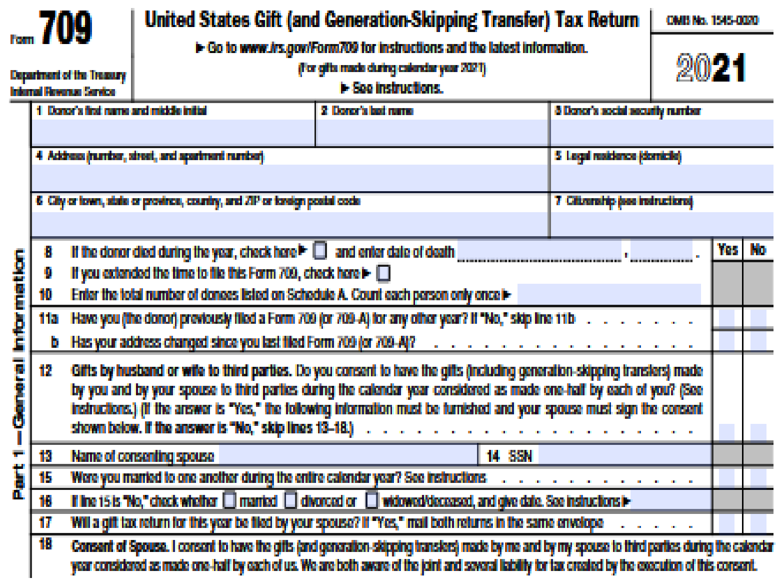
Regardless of what type of asset is gifted and how it transfers, it is good to keep a **written record** of the gift. Documenting the gift is important to avoid misunderstandings about what asset was gifted and helpful if there is an IRS audit. The written record should include a description of the gifted asset, the value of the gift, who is receiving the gift, and the date of the gift. For cash, consider using a check as further record of the gift. The person receiving the gift should also date and sign documentation to confirm that they have accepted the gift.

GIFTS AND TAXES

The gift tax. The federal government and many states assess a tax on gifts, but Ohio does not have a gift tax. The federal gift tax was developed to prevent individuals from avoiding federal estate taxes by gifting away significant assets prior to death. For this reason, it is the giver of a gift who is responsible for paying the gift tax. The gift tax begins at 18% on the first $10,000 and increases by 2% every additional $10,000, to 40% on gifts over $1 million. A giver uses IRS Form 709, pictured here, to document a gift that may be subject to gift tax.


Form 709 United States Gift (and Generation-Skipping Transfer) Tax Return OMB No. 1545-0020

Department of the Treasury Internal Revenue Service

▶ Go to www.irs.gov/Form709 for instructions and the latest information.
(For gifts made during calendar year 2021)
▶ See instructions.

2021

Part 1—General Information

1 Donor's first name and middle initial | 2 Donor's last name | 3 Donor's social security number

4 Address (number, street, and apartment number) | 5 Legal residence (domicile)

6 City or town, state or province, country, and ZIP or foreign postal code | 7 Citizenship (see instructions)

		Yes	No
8	If the donor died during the year, check here ▶ ☐ and enter date of death ______, ______.		
9	If you extended the time to file this Form 709, check here ▶ ☐		
10	Enter the total number of donees listed on Schedule A. Count each person only once ▶		
11a	Have you (the donor) previously filed a Form 709 (or 709-A) for any other year? If "No," skip line 11b		
b	Has your address changed since you last filed Form 709 (or 709-A)?		
12	Gifts by husband or wife to third parties. Do you consent to have the gifts (including generation-skipping transfers) made by you and by your spouse to third parties during the calendar year considered as made one-half by each of you? (See instructions.) (If the answer is "Yes," the following information must be furnished and your spouse must sign the consent shown below. If the answer is "No," skip lines 13–18.)		
13	Name of consenting spouse — 14 SSN		
15	Were you married to one another during the entire calendar year? See instructions		
16	If line 15 is "No," check whether ☐ married ☐ divorced or ☐ widowed/deceased, and give date. See instructions ▶		
17	Will a gift tax return for this year be filed by your spouse? If "Yes," mail both returns in the same envelope		
18	Consent of Spouse. I consent to have the gifts (and generation-skipping transfers) made by me and by my spouse to third parties during the calendar year considered as made one-half by each of us. We are both aware of the joint and several liability for tax created by the execution of this consent.		

Exceptions to the gift tax. The good news is that federal law grants many exceptions from the gift tax. A gift to a spouse or a political or charitable organization is not subject to the tax, nor is tuition or medical expenses paid for another. Additionally, federal law allows a certain value of gifted assets to pass free of gift taxes, referred to as the "annual exclusion." Gifts in excess of the annual exclusion may also be given tax free if they count toward the "lifetime exemption" from estate tax. Here's how these two types of gifts work:

1. **Annual exclusion gift.** The annual exclusion gift is truly a "free gift." A person may gift up to $16,000 annually to an unlimited number of people. These annual exclusion gifts have no gift or estate tax implications. Neither the person who gives or the person who receives the gift is subject to a tax. As an example, a person can gift $1 million tax free by giving the annual exclusion gift of $16,000 to 63 different individuals. Note that federal law indexes the annual exclusion gift amount and occasionally increases it by $1,000 as it did in 2022, when it increased from $15,000 to the current $16,000.

2. **Lifetime exemption gift.** Many people are surprised to learn that large gifts can also be free from gift tax by counting toward a person's lifetime exemption from federal estate tax. The lifetime exemption is the amount of wealth a person can have at death that is not subject to federal estate taxes, as determined by Congress and indexed and increased each year. For 2022, the amount is $12.06 million but in 2026, the current federal estate tax law is set to sunset and the exemption will be reduced by one-half.

Federal law allows the lifetime exemption to be "used up" during a person's lifetime. The amount of a gift that exceeds the $16,000 annual exclusion can reduce the giver's lifetime estate tax exemption by that amount when they die. If not, the amount of a gift over $16,000 can be subject to gift tax rates that start at 18% and increase to 40% on gifts over $1 million. People often choose to avoid the gift tax and reduce their lifetime exemption when making gifts over the annual exclusion amount.

The best way to explain these two important gift tax exceptions may be by using examples. **Consider the following examples**:

Example 1. John's net worth is $10 million at death and his lifetime exemption is $12.06 million. John's estate owes no estate taxes because his net worth is less than his lifetime exemption.

Example 2. John gives a single gift of $1 million to Daughter while alive and counts it toward his lifetime exemption. John's net worth at death is $10 million. The gift to Daughter was $984,000 over the $16,000 annual exclusion, which reduces his $12.06 million lifetime exemption by that amount to $11.076 million. John's net worth of $10 million at death is still less than his remaining lifetime exemption, so his estate will owe no estate taxes. The $1 million gift to Daughter was essentially a free gift because his net worth remained under the lifetime exemption.

Example 3. Same scenario as Scenario 2, but John dies with a net worth of $12 million. After the gift to Daughter, John's remaining estate tax exemption is $11.076 million. Now his net worth exceeds his remaining lifetime exemption by $924,000, so John's estate will owe federal estate taxes on that amount. John's large gift in this scenario had federal estate tax implications. Had he given Daughter the $1 million in smaller gifts to Daughter and her family over the years, John could have reduced the amount of

EFFECT OF GIFTING ON TAX BASIS

An asset's tax basis is generally the purchase price or its value when inherited, less depreciation taken. For example, a tractor purchased for $100,000 with $60,000 depreciation taken has a tax basis of $40,000 remaining.

The tax basis of an asset has significant tax implications. The higher the tax basis, the more depreciation can be taken and the less taxes owed when sold. Using the above example, if the tractor is sold for $70,000, the $40,000 tax basis is not taxed, only the $30,000 gain (sale price – tax basis) is taxed. The higher the tax basis, the less taxes are upon sale.

As noted above, the tax basis is usually established at time of purchase or inheritance. This is known as a "step-up" in tax basis because the tax basis is stepped-up to either the purchase price upon purchase or the fair market value upon death of the owner. This step-up in tax basis is particularly important when an asset is inherited because **when an asset is gifted, a step-up in basis does not occur**. For estates with no estate tax liability, an inherited asset with no estate tax also receives a full stepped-up tax basis. The person inheriting can re-depreciate the asset or sell the asset and pay no taxes on the sale, if sold for no more than the stepped-up tax basis. **Consider another example**:

> Bill inherited the tractor above from his father's estate. Prior to his father's death, the tractor had a tax basis of $40,000. The tractor appraised for $80,000 at the time of father's death, so Bill receives the tractor with a stepped-up tax basis of $80,000. Bill can either depreciate the tractor and offset $80,000 of income or sell the tractor for $80,000 and pay no tax on the sale. If Bill's father would have gifted the tractor to Bill during life, Bill would have received it with the lower $40,000 basis. From a tax perspective, Bill was better off inheriting the tractor rather than being gifted the tractor.

As these examples show, there can be negative consequences to gifting assets. Before gifting an asset, be sure to analyze all the tax implications of the gift. You may find that passing the asset by updating your estate plan is a better strategy for your heirs.

USING GIFTING STRATEGIES IN A FARM TRANSITION AND ESTATE PLAN

While gifting is not always the best tax strategy for farm transition plans, there are times when its advantages outweigh the loss of a step-up in tax basis. Gifting can be, and often is, an important part of a plan. The following scenarios illustrate situations where gifting can be a good option:

Transferring a depreciating asset. Sometimes the older generation owns machinery, equipment, livestock, or other assets that will lose value over time. Owning these types of assets also carries with them some degree of liability exposure. If an owner does not need income from the assets, it can make sense to transfer the assets now rather than upon death. In this situation, transferring the assets during life to remove the challenges of ownership outweighs the lost step-up in tax basis.

Gifting appreciating assets. For people who are close to or over the estate tax exemption, gifting appreciating assets can be a good strategy. If the asset is gifted now, the future appreciation of the asset is transferred out of the giver's estate. For example, a farm is gifted that is worth $1 million today but is expected to have a significant increase in value. When the value of the farm doubles, the additional $1 million in appreciation occurs in the giftee's estate rather than the giver's estate. The gift causes a loss of a stepped-up tax basis, but it is probably well worth it to avoid a 40% estate tax on the $1 million appreciation.

REVIEW GIFTING WITH YOUR LEGAL AND TAX PROFESSIONALS

Gifting can be a good tool to help build a farm transition plan, but sometimes it should be left in the toolbox. Be sure to have a discussion with your attorney and tax advisor before making any significant gifts. A thorough analysis can reveal tax implications for both you and the person receiving the gift.

REFERENCES

26 U.S. Code Subtitle B Chapter 12, Gift tax
https://www.law.cornell.edu/uscode/text/26/subtitle-B

26 U.S. Code Subtitle A Chapter 11, Estate tax
https://www.law.cornell.edu/uscode/text/26/subtitle-B/chapter-11

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USING BUSINESS ENTITIES IN FARM TRANSITION PLANNING

A formal business entity can be a valuable tool in farm transition planning. Many attorneys advise forming a formal business entity to limit liability and manage taxes, but an increasing number of agricultural attorneys have found that business entities are excellent tools for transitioning the farming operation to the next generation. We explain business entities and how they can be used in farm transition and estate planning in this bulletin.

BUSINESS ENTITY BASICS

The farm business can be an informal structure, such as a sole proprietorship, or can be formally organized, such as a corporation or limited liability company. Each type of entity has its own set of liability protections, tax issues, ownership transfer processes, and other characteristics.

Sole proprietorships and general partnerships. Sole proprietorships and general partnerships are the simplest business entities, and according to the U.S. Census of Agriculture, the majority of U.S. farms are one of these two types. They are business entities that generally require no filing of paperwork with a state. While the details may vary from state-to-state, the characteristics of these types of entities are fairly consistent nationwide. They afford no liability protection to the owners because any liabilities of the business are also the personal liabilities of the owner, and taxes are assessed directly to the sole proprietors or the partners at individual tax rates.

By default, if there is no formal business entity, an individual who owns lands, equipment, and other goods to make a profit will own those assets as a **sole proprietor**. The sole proprietor is the business, and the business is the sole proprietor. The business has no existence beyond the sole proprietor, so when the proprietor dies, the business ends and the assets are divided up through the proprietor's estate. A sole proprietorship has limited usefulness in a transition plan because entities that are separate from the owners are best suited for farm transition planning.

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If two or more people own land, equipment, and other goods to make a profit with no formal business entity, then they own the business as general partners in a **partnership**. A partnership may or may not have a formal written partnership agreement. In either event, Ohio's Uniform Partnership Act provides laws that govern partnerships in Ohio and provides default rules if the partners haven't addressed them in a partnership agreement. In the eyes of the law, a partnership is a "person" and can own assets and conduct business as a person would. Partnerships are typically more flexible and less formal than corporations. A partnership may and often does continue after the death of a partner. For these reasons, a partnership can be an effective component of a farm transition plan.

The simplicity of sole proprietorships and general partnerships come with the tradeoff of **no liability protection**. The sole proprietor is personally responsible for any liability of the business because there is no separation between the proprietor and the business. In a general partnership, all partners can be personally liable for any losses, debts, or mistakes related to the business and the other general partners. For example, if one partner signs a contract for the partnership, the other partners are bound to and personally liable for the contract.

Corporations. A corporation is an organized business entity with a separate legal status from its owners. Corporations have the right to buy and sell property, carry debts, enter into contracts, and more. This is why we hear the phrase "corporations are people." Shareholders own the corporation and typically elect a board of directors who in turn select officers to run the day-to-day operations of the corporation. Shareholders have limited liability and are only liable for losses up to their investment in shares.

State laws governing corporations can be rather complex and burdensome. The shareholders and board of directors must hold annual meetings and keep detailed records of meetings and activities. Corporations are typically governed by majority rule, such that the owners of 51% of voting stock decide how the corporation operates.

There are two primary types of corporations: C-corps and S-corps.

1. **C-corps** are taxed directly, but shareholders are also taxed on any dividend they receive, which results in double taxation. When people think of a corporation, they often think of C-corps.
2. **S-corps** are a sub-set of corporations with special rules. People often refer to these as closely held corporations because they may have no more than 100 shareholders and have pass through taxation. S-corps may not have corporate shareholders and can only issue one class of stock.

Limited liability companies. A limited liability company (LLC) combines features of partnerships and corporations, and many attorneys describe the LLC as the best of both worlds. Like a corporation, an LLC is an organized business entity that has a legal status separate from its owners with personal liability protection for the owners. Like a partnership, owners of an LLC can create flexibility in how the LLC is governed. For taxation, LLCs may choose to be taxed directly like a C-corporation or to pass taxes to the members as in a partnership or S-corporation.

LLCs are the entity of choice for most new farm businesses, for many reasons. We discuss the usefulness of LLCs in transition planning in the rest of this bulletin, but be aware that there are times when a partnership or corporation may be a better choice than an LLC. The concepts we discuss below can apply similarly to partnerships and corporations.

USING THE LLC FOR FARM TRANSITION PLANNING

LLCs allow for considerable creativity when designing a farm transition plan. Here are several roles an LLC can play in carrying out the goals of a farm transition and estate plan.

1. Protecting farmland

No asset is more important to a farmer than the land. An LLC can protect the land for future generations by preventing any one family member from forcing the sale of the land and making it difficult to transfer land unless the family collectively agrees to do so. But leaving land to family members outright to own jointly exposes family land to risk**.** That's because Ohio's **partition law** allows a co-owner of land to ask the court to sell the land and divide sale proceeds among the owners. A co-owner can seek partition regardless of what share they own, as can successor owners and creditors. With partition rights, the original co-owners and their spouses, heirs, and creditors all have the ability jeopardize the goal of keeping land in the family.

An LLC removes the risk of partition. Ohio law grants partition rights only to co-owners of land, not to co-owners of an LLC. When land is placed in an LLC, partition rights are extinguished because the LLC owns the land rather than the individuals co-owning the land. The owners of the LLC do not have the ability to use the partition law to force the sale of the land. **Consider the following examples!**

*Example 1***.** Mom and Dad want to leave their farmland to their three children. They have a simple will that gives all the land to the three children as co-owners. After the parents die, Arthur, one of the children, decides that he would rather have money than continue to own the land. The other two children are unable or unwilling to buy Arthur out at his asking price, so Arthur files a partition action. The court orders the land to be sold at a Sheriff's sale and the sale proceeds to be divided among the three children. The family no longer owns the land.

Example 2. As above, Arthur is a co-owner of the land given by Mom and Dad to the three children. Arthur gets into financial trouble and must sell his one-third of the land to pay his creditors. Arthur files for a partition so that he can receive his value of the land in cash to pay the creditors. The family no longer owns the land.

Example 3. Mom and Dad put their land in an LLC. Their three children inherit the LLC. Now, when Arthur wants to sell, he does not have partition rights. Arthur is an owner of the LLC, not a direct owner of the land. The only way Arthur can cash out is if one of the other owners agree to purchase his ownership. If Arthur gets in financial trouble, his creditors do not have partition rights and cannot force the sale of the land. At most, the creditors are only entitled to Arthur's share of the profits from the LLC. The family continues to own the land.

2. **Discounting value**

An LLC can be used to decrease the value of assets. This is important when a person's net worth exceeds the federal estate tax exemption. All wealth exceeding the federal estate tax exemption is taxed at 40%, so it is important to make all efforts to minimize the negative effect the estate tax can have on the goal of transitioning the farm to the next generation.

An LLC can decrease net worth with a concept called **discounting**. Essentially, the value of the ownership in a closely held company is discounted to be less than the value of the assets in the company. This is due to minority ownership, shared management, and transfer restrictions of the LLC ownership, all factors that reduce values. Discounts can be as high as 30-40%, which can minimize the risk of estate taxes being assessed on farm assets. **Consider this example**:

Mom and Dad own a farm and their net worth exceeds the federal estate tax exemption by $1 million, so their heirs will owe $400,000 in estate taxes upon their death.

Mom and Dad own 500 acres of land valued at $5 million. They put the land in an LLC, and each holds 50% ownership in the LLC. They also set up the LLC so that a decision requires a majority vote and ownership interests can only be transferred to direct family members. Neither Mom nor Dad have majority ownership or control, and each is limited as to whom they can transfer their ownership – all important factors to obtaining a discount.

Let's assume a 35% discount applies to Mom and Dad's LLC ownership interest because the discounting factors exist. Now, instead of owning land valued at $5 million, they co-own an LLC worth $3.25 million. Mom and Dad have reduced their net worth by $1.75 million by placing their land in the LLC. They have given up little to receive a significant reduction in the value of their estate.

3. **Designating management**

An LLC can also designate the future managers of the farming operation or its assets. Not all beneficiaries of a transition plan may be qualified or willing to manage the farm's assets, or maybe the beneficiaries don't get along well and wouldn't make joint asset management decisions easily. An LLC can address these issues by determining who will have management and decision-making authority. **Consider this example:**

Mom and Dad want their three children to jointly inherit their farmland. Two children live out-of-state and have never been involved with the farm while the third child lives locally and has been involved. Mom and Dad's transition plan transfers the land to an LLC, makes the children owners of the LLC, and designates the local child to be the manager of the LLC.

The management provisions help ensure that the land will be managed properly and the out-of-state children's unfamiliarity with the land will not cause disruptions or poor decision making.

4. **Removing the need for a trust**

Many farm transition plans include a trust as the primary estate planning document, as we explain in other bulletins in this series. Using a trust can avoid probate and include terms and conditions for the distribution of assets at death. But in some cases, an LLC can negate the need for a trust. Like a trust, an LLC can avoid probate and contain ownership restrictions, management responsibilities and other terms and conditions. An LLC may also save time and legal fees. An LLC can replace a trust, or sometimes LLCs and trusts are used in combination in a transition plan. Before assuming that you need a trust, explore the possibility of using business entities instead. **Consider this example**:

Mom and Dad want their children land to inherit their farmland. They don't want the land sold outside of the family and want one specific child to manage the land. Instead of a trust, Mom and Dad establish an LLC with their required terms and conditions and make ownership of the LLC "transfer on death" to their children. The children inherit the LLC without going through probate and are subject to the transfer and management terms of the LLC. Mom and Dad accomplished their transition plan without the use of a trust.

5. **Balancing assets between heirs**

LLCs can also be used to balance assets between farming heirs and non-farm heirs. For farm families, it can be difficult to provide a fair inheritance to non-farm heirs without including at least some farm assets. Farm assets, such as land, can be put into an LLC. Then, the non-farm heirs are provided ownership in the LLC, perhaps even a majority. The farming heir is provided at least a small percentage of ownership and may have the ability to prevent the sale of the land or have an option to buy out the non-farm heirs. LLCs can provide non-farm heirs ownership of farm assets without the risk of those assets leaving the farm. **Consider this example:**

Mom and Dad own a farm business that includes machinery, livestock, and land. They have three children–Bill, Chris, and David. Only Bill is involved with the farm and will continue it after Mom and Dad's deaths. Like most farmers, Mom and Dad's wealth is almost entirely wrapped up in the farm. If Bill were to inherit all the farm assets, little value would be left for the inheritance of Chris and David. However, if Chris and David were to inherit two-thirds of the farm assets, it could jeopardize Bill's ability to continue a viable farming operation.

Mom and Dad establish an estate plan where Bill will inherit all the machinery and livestock. They form an LLC for the land and grant ownership shares to Bill, Chris, and David, with Chris and David receiving a larger share to offset the machinery and livestock Bill received. The LLC names Bill as the Manager and allows the land to be leased back to Bill.

In this scenario, the land LLC allows Chris and David to inherit farm assets without being able to interfere with Bill's farming operation. Chris and David will receive their share of the land rent, but Bill will retain control over the land. This strategy provides farm assets to non-farm heirs while leaving control of the farm with the farming heir.

FORMING A BUSINESS ENTITY

The internet is full of advice and fill-in-the-blank forms for forming a business entity. It's a decision that requires more than an internet search, however. Your attorney is a necessary resource not just for selecting an entity that carries out your goals, but for designing your entity so that it does what you want it to do. An attorney can tailor the legal documents for your business entity to your goals, ensuring that they contain the appropriate provisions and mechanisms to achieve those goals.

Choosing the right business entity for you, your family, and your farm is an important step in the farm transition planning process. An LLC is one type of entity that can help protect farmland, minimize estate tax risk, designate management authority, and keep assets out of probate. If any of these goals are in your farm transition plan, be sure to review them with an attorney who can help you design the entity that fits your plan for the future of your farm.

REFERENCES

Ohio Revised Code, Title 17, Corporations-Partnerships
https://codes.ohio.gov/ohio-revised-code/title-17

AUTHORS OF THE PLANNING FOR THE FUTURE OF YOUR FARM SERIES

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Keeping Farmland in the Family

Legal strategies to keep farmland in the family for future generations

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Keeping Farmland in the Family

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Using this information

This publication identifies risks that can affect the goal of keeping farmland within a family and explains legal strategies that can reduce those risks. Please do not use this information to substitute for individual professional legal advice. **The information is based on Ohio law**, but the concepts are broadly applicable across the United States. Even so, it is important to work with a competent attorney in the state where the farmland is located to how a state's laws affect a legal strategy.

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Introduction

Handing down the heritage that comes with owning farmland is a common goal of farm families. But there are many risks that can take farmland out of the family and separate future generations from a farm heritage. For those who want to keep farmland in the family, it is necessary to address the risks through planning. The first step in the planning process is to understand those risks that can cause farmland to leave the family, and the second step is to adopt legal strategies to reduce those risks. This publication offers information on each step of the planning process. As with any legal decision making, be sure to consult a private attorney. If keeping farmland in the family is an important goal, use this information to begin the planning process and use an attorney to help finalize a plan to accomplish the goal.

1. The Risks to Keeping Farmland in the Family

Unfortunately, there are many risks that can cause farmland to leave a family. The type and severity of risks to a family should be analyzed and understood. Assessing a family's risks can help with identifying the strategies to mitigate the risks. The following explains the most common risks and provides examples to illustrate how the risk can result in a loss of farmland for a family.

Partition

It is likely that more farmland involuntarily leaves farm families through partition than in any other way. A partition law allows someone who co-owns property with another (a co-tenant) to force the division or sale of the property. Any co-tenant, regardless of their percentage of ownership, may initiate a partition action. Ohio is one of many states that has a partition law.[1]

The concept of partition is that it provides a remedy to a co-tenant who does not wish to remain an owner of real estate. Without partition rights, a co-tenant might never be able to divest themselves of ownership of the real estate if other co-tenants don't agree to buy their share or sell the entire property. Generally, the law does not favor prohibiting an owner from being able to sell or transfer assets they own. Partition provides the solution for a co-tenant who wants to sell their interest in real estate despite disagreement by other co-tenants.

[1] Ohio's partition laws are in Section 5307 of the Ohio Revised Code. See a compilation of all state partition laws on the National Agricultural Law website at https://nationalaglawcenter.org/state-compilations/.

Partition is also somewhat of a dispute resolution tool because Ohio law does not have rules for how co-tenants are to manage their real estate together. For example, Ohio law does not state how owners jointly holding property can resolve differences about how to manage the property. This means an owner with a minority interest could prevent management actions for leasing, selling, or mortgaging the land even if the majority landowner wants to do so. Partition laws resolve management disputes among co-tenants by forcing a sale or division of the land if the co-tenants cannot agree on how to manage it.

Consider the following example.

John, Karen, and Larry own land jointly. John and Karen own 45% each and Larry owns 10%. John and Karen want to sell the land but Larry refuses. John and Karen's combined 90% interest cannot out vote Larry's 10% interest. Without Larry's consent, John and Karen cannot sell the land. But John or Karen could file for partition and force the sale of the land without Larry's approval.

The risks of partition. Any time two or more people own real estate together, there is a risk of partition. Any co-tenant can file for partition, even if they own only a small percentage of the property. Future owners will also have partition rights, and as farmland moves from one generation to the next and the number of owners increase, so does the risk of partition. When ownership transfers to the surviving spouse of an owner, particularly one who may not have any attachment to the land, partition risks can also increase significantly.

Consider the following examples.

Example 1

Amy, Bob, and Charlie inherit the family farmland from their parents. All three siblings are equal, one-third co-tenants of the land, which has been in their family for many generations. After owning the land for a few years, conflict arises among the three owners about how the land should be managed. Amy, frustrated that her brothers do not respect her suggestions for the use of the land, files a partition action. The land is then sold at auction by order of the court and the sale proceeds are divided among the three siblings.

Example 2

Same facts as Example 1 except Amy dies and her husband Dale receives her one-third ownership interest. Amy's parents assumed Amy's share in the land would go to her children but Amy never bothered with an estate plan, so Dale receives the land. Dale has no ties to the farmland and does not understand what the big deal is about owning farmland. Dale prefers that the land be sold so he can receive his one-third of the value and buy the boat he has always wanted. He files a partition action, the farm is sold at auction, and he receives one-third of the value.

As these two examples show, it is relatively easy for a co-tenant to use partition to force the sale of the land. Also, it is not just known owners who cause partition risk. Partition rights attach to any future owner who ends up on the deed, including non-family members like Dale.

Partition rights are a real and omnipresent threat to keeping farmland in the family. Even a small percentage owner of a large farm may have an incentive to initiate a partition action. Landowners should be aware of the concept of partition so that they can understand and evaluate the risks of co-tenancy and plan accordingly to minimize the risk of partition.

> *"Partition rights are a real and omnipresent threat to keeping farmland in the family."*

The partition process. In Ohio, partition occurs through a lawsuit filed with the common pleas court of the county where the real estate is located.[2] The plaintiff, who is the co-tenant initiating the partition, files a petition with the court asking for the land to be partitioned. The petition must include the identity of all co-tenants and a description of the property. Each co-tenant defendant has an opportunity to respond to the partition. Like all litigation, the parties should engage legal counsel to assist them in the partition process.

After the partition has been filed and all parties notified, the court is required to appoint at least one disinterested person, referred to as the "commissioner," to oversee the partition action.[3] The commissioner must view and examine the property and determine if the property can be physically divided without the loss of value.[4] Due to the unique nature of farmland property and factors such as drainage, soil type, road frontage, and development potential, it can be difficult for a commissioner to physically divide the property fairly among the co-tenants. Instead, the court may order the property to be sold and the proceeds divided. In that case, the commissioner must establish the value of the property by appraisal.[5] Any of the co-tenants then have the option to purchase the property at the appraised value. A co-tenant may pay the purchase price in three installments of one-third cash at purchase, one-third in one year, and one-third in two years.[6] If no co-tenants wish to purchase the property, the court will order it sold.

The property can be sold at Sherriff's sale or at public auction. Usually, the parties will agree to sell at public auction in hopes of getting a higher price for the property. A properly advertised public auction is more likely to get a higher price than an unadvertised sheriff's sale. The sale price must be at least two-thirds of the appraised value.[7] Upon completion of a successful auction and receiving the payment, the sheriff will execute a deed to the purchaser.[8] Net proceeds from the sale are divided among the co-tenants according to their proportion of ownership.[9]

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[2] ORC 5307.02
[3] ORC 5307.04
[4] ORC 5307.06
[5] ORC 5307.09
[6] ORC 5307.10
[7] ORC 5307.12
[8] ORC 5307.13
[9] ORC 5307.14

Divorce

A well-known statistic is that one-half of all marriages end in divorce. While there is some debate as to the accuracy of this statistic, there is no doubt that many marriages do end in divorce. With a divorce comes the division of assets and the risk that farmland will be sold to provide an equitable result for the divorcing couple, or that a spouse not involved in the family farm will receive the farmland.

According to Ohio law, marital assets are to be divided "equitably" in the event of a divorce.[10] Equitable does not necessarily mean equal although an equal division of marital assets between the spouses is often the result. Divorces can be especially threatening to farmland because of the "land rich, cash poor" dilemma for farmers. In a farm divorce, it is usually not equitable for one spouse to receive all the farm assets if there are not sufficient non-farm assets for the other spouse. Thus, both spouses may receive farmland in the divorce settlement. Either spouse could sell the land out of the family.

It is important to note that only "marital" assets are subject to the equitable division between spouses in a divorce. Non-marital assets, referred to as "separate" assets, are retained by the spouse who individually owns the asset.

Separate assets include the following:

- Property acquired by a spouse prior to the date of the marriage.
- Passive income and appreciation from separate property received by a spouse during the marriage.
- An inheritance received by a spouse during the marriage.
- A gift received by a spouse during the marriage.

The above list would seem to make it an easy exercise to determine which assets are marital and which are separate in a divorce situation. However, like many legal issues, easy is not often the case. That's because Ohio law also provides that income or appreciation on separate property can *become a marital* asset. The law includes as marital property:

> "… all income and appreciation on separate property, due to the labor, monetary, or in-kind contribution of either or both of the spouses that occurred during the marriage."[11]

So, it is possible for an asset to be partially separate (the property) and partially marital (the income and appreciation on the property).

Consider the following example.

Andy and Beth are farmers in the process of divorcing. Shortly after they were married, Beth inherited a 100-acre farm from her grandmother. When she inherited the farm, it was valued at $600,000. A few years after inheriting the farm, Andy and Beth's farming operation paid for and installed $80,000 of drainage tile on the farm. The current value of the farm is $1 million.

In this example, the farm was Beth's separate asset upon inheritance. However, the tile that improved the quality and value of the farm was

[10] ORC 3105.171

[11] ORC 3105.171

a result of Andy and Beth's joint farming operation. Andy likely has a valid claim that at least part of the $400,000 increase in value is a marital asset due to the tile installation.

Perhaps Andy further argues that most of the increase in value was due to the fertilizer, tillage and other soil improvements made while Andy and Beth farmed the land. It is in Andy's interest to make the $400,000 increase in value a marital asset. Conversely, Beth could argue that the increase was not a result of the marital farming operation but was merely a passive value increase due to market pressure. It is in Beth's interest to argue the $400,000 increase as her separate asset.

As this example illustrates, an asset that is initially a separate asset can become, at least in part, a marital asset. Both Andy and Beth have valid arguments. It is not hard to imagine how much time and legal fees could be spent resolving or litigating the issue in a contentious divorce.

Co-mingling assets can also cause a separate asset to become a marital asset. If the spouse owning the asset voluntarily allows the other spouse to become an owner of the asset, it is likely to become a marital asset. Using the example above, after Beth receives the farm, she adds Andy's name to the deed as co-tenant. Because she voluntarily added Andy to the deed and gave him half ownership, Beth has likely changed the property from a separate to a marital asset.

Another example might be that Beth receives a $100,000 inheritance from her grandmother. Beth deposits the money in an investment account owned by both her and Andy. By co-mingling the inherited money with other money owned jointly with Andy, Beth has probably made the $100,000 inheritance a marital asset. If Beth would have deposited the money in an account owned only by her, the inheritance would have remained a separate asset. While co-mingling does not automatically make an asset become marital property, the spouse owning the asset should avoid co-mingling if wanting to keep the asset separate.

Assets acquired *during* a marriage will almost always be considered marital property. This is true even if one spouse provided little or no contribution towards the acquisition of the asset. Ohio law considers marriage to be a sort of equal partnership regardless of the contribution of the spouses. For example, farmland purchased during the marriage will be a marital asset even if only one spouse operates on the farmland and the other spouse is not involved with the land or operation.

A **prenuptial agreement** can help alleviate the issues of marital assets. This type of agreement entered into prior to marriage designates what assets they are bringing to the marriage, what assets will be separate, and what assets will be marital. Especially for people who have accumulated some wealth prior to marriage, a prenuptial agreement is a good option to avoid future disputes of the nature of assets in a marriage and potential risks to farmland.

Debt

The inability to repay debt can cause farmland to leave the family. Farmland is commonly used as collateral for loans. Lenders favor farmland to secure their loans because it is a safe, low risk asset that cannot be moved or hidden like other assets, does not depreciate, and generally holds its value. When a debtor defaults on a debt, the lender has the right to foreclose on the collateral. Many family farms have been lost to foreclosure through mortgages and judgment liens.

Mortgages. One way to foreclose on farmland is through a mortgage that secures a loan. A mortgage is a legal instrument that gives a lender the right to foreclose or sell the property if the property owner defaults on the loan. The mortgage is similar to a deed in that its transfers rights in the property to the lender and is recorded. A mortgage can be placed on any single parcel of land or many parcels of land.

A mortgage includes provisions as to when the lender is entitled to foreclose on the property. Typically, a breach of payment under the corresponding promissory note executed with a mortgage will entitle the lender to foreclose. The foreclosure process is similar to a lawsuit in that the lender files a complaint with the court. Assuming the court finds the debtor is in default, the court issues a foreclosure judgment and the property is sold. Any funds remaining after the lender is paid and costs are reimbursed are given to the property owner.

Judgment liens. Even land without a mortgage on it is at risk of foreclosure. A mortgage makes it easier for a lender but it is not the only means to force the sale of land for debt repayment. Whenever a debtor is in default, the lender can file a lawsuit against the debtor to seek payment of the debt. If the lender prevails in the lawsuit, the court can issue a judgment lien on any real estate owned by the debtor and the lender can foreclose on the property that is subject to the judgment lien. The process of filing a lawsuit and using a judgment lien to foreclose on property may take longer and be more complicated than a mortgage, but it has the same result as a mortgage.

Consider the following example.

Charlie owes the fertilizer company $200,000 and is unable to pay his bill. The fertilizer company files a lawsuit against Charlie and is awarded a judgment in its favor by the court. The court then places a judgment lien on Charlie's farm. The fertilizer company uses the lien to foreclose on the farm and force it to be sold at auction. The farm brings $500,000 at auction. From the sale proceeds, legal and court costs of $25,000 are paid and the fertilizer company receives its debt repayment of $200,000. Charlie receives the remaining sale proceeds.

In this example, the farmland was sold even though there was no mortgage on the land. A lender or vendor with an outstanding debt can use a lawsuit and judgment lien to force the sale of farmland to repay the debt.

Long-term care costs

Long-term care (LTC) costs are a significant threat to family farmland. Average annual LTC facility costs in Ohio are $90,000. A long-term stay can deplete financial resources and force a sale of farmland to pay for the care.

While a farmer has little control over the LTC they may need, there are ways to reduce the risk of LTC to farmland. For example, LTC insurance and gifting farmland to family members are two strategies that can protect the land. Each strategy has advantages and disadvantages, and there are no easy solutions.

For a detailed discussion on LTC risk, see our publication, *Long-Term Care and the Farm.*[12] This publication explains common strategies to mitigate LTC risk. Understanding LTC and implementing a plan to help mitigate risk is important to protecting farm assets, especially the land.

Medical costs

As with LTC costs, medical costs are another threat to keeping farmland in the family. While most people carry medical insurance of some type, policies vary greatly in the extent of coverage provided. Even with insurance, a serious illness or injury can cause significant out-of-pocket expenses and debts.

A doctor or hospital carrying outstanding medical debt becomes a creditor, and the law provides mechanisms for them to receive payment. As discussed above for other types of debt, a medical creditor can file a lawsuit for outstanding medical bills, obtain a judgment lien, and use the lien to foreclose on farmland. Unexpected medical costs, and insufficient non-farmland assets to cover them, present another risk for losing family farmland.

Poor estate planning

Poor estate planning can also cause farmland to leave the family. When heirs who inherit farmland have different goals for the land and the estate plan doesn't place any restrictions on their farmland ownership, the land is at risk. For example, an heir who wishes to "cash out" their land has a very different goal than an heir who wants to keep land in the family for future generations. If the estate plan doesn't prevent cashing out, an heir who wants to sell land can do so. And if the heir is a co-tenant, the other co-tenant heirs will lose the land. Either way, the land will leave the family because there wasn't a plan to prevent the loss.

Of all the risks identified, poor estate planning is the easiest risk to manage. An estate plan that keeps the land in the family can be implemented with a modest investment of time and money. All of the strategies discussed in the next section can be incorporated into an estate plan and used to protect the farmland. Meeting with an attorney knowledgeable in farm estate and succession planning strategies who recognizes the goal of keeping land in the family is a good place to start to reduce the risk of poor estate planning.

[12] Available at https://farmoffice.osu.edu.

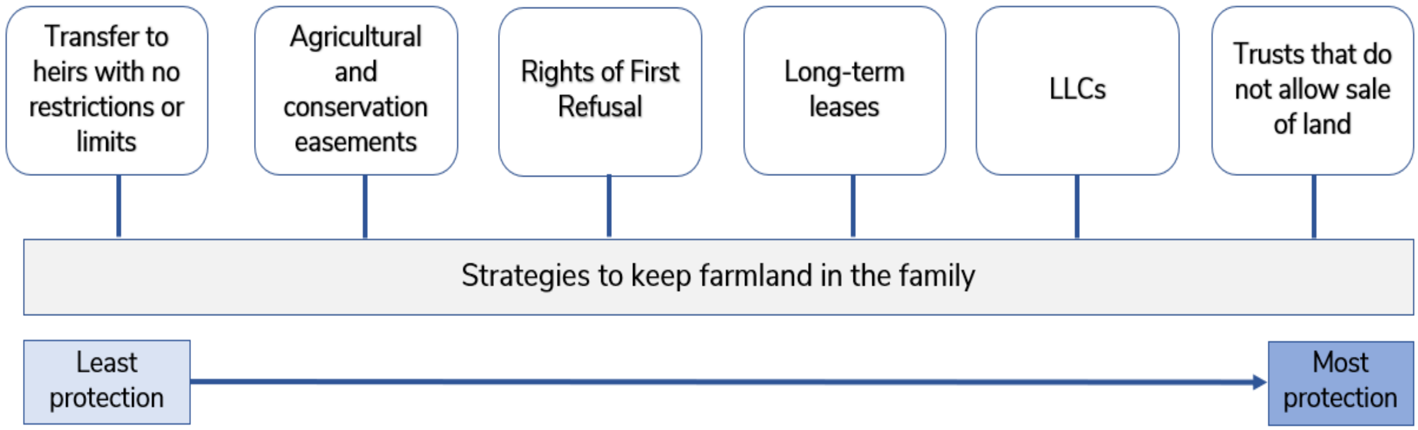
2. Strategies to Keep Farmland in the Family

Part One identified many, but not all, of the risks that can cause farmland to leave the family. For every risk, there is a strategy that at least lessens the exposure of farmland to that risk. Risks can never be eliminated but good planning can help make a risk the exception rather than the rule.

Before deciding which strategy is best, a family must consider their goals for the land and the family. For example, one landowner may not worry very much about the land staying in the family. While this approach is rare for farm families, it can happen. On the other hand, another landowner may not want land to go out of the family for any reason. Somewhere between the two extremes is the goals of discouraging the land from leaving the family but not completely tying the hands of future generations.

Diagram 1 on the following page illustrates this spectrum of goals and provides a preview of the different strategies that follow the goals along a spectrum of protection. The strategies on the left side of the diagram are less protective and can work for those who don't want to put many restrictions on the land – the "they can do what they want with the land" approach. Strategies on the right side are the most protective and would keep land in the family for at least a generation or two. In between are moderately protective strategies for the goal of keeping the land in the family, but they do not make it impossible for the land to leave the family. The following discusses all but the self-explanatory "no restrictions or limits" strategy on the left side of the spectrum. Examples demonstrate the strategies in family farmland situations.

Diagram 1. Spectrum of strategies to keep farmland in the family



Trusts

The primary purpose of a trust is usually to transfer assets from the trust's creator (grantor) to the grantor's beneficiaries. A trust allows for much flexibility and creativity in estate planning and can give a grantor control of assets "from the grave." In addition, a trust can hold and manage assets for future generations. For these reasons, a trust can be very helpful when the goals and objectives of the current landowner are to prevent the land from leaving the family.

Consider the following example.

Judy owns farmland that has been in her family for five generations. She wants to make sure her grandchildren will have an opportunity to own the farmland someday. She is concerned that her children may sell the farmland when they inherit it or may get into financial trouble and be forced to sell it. The land is cash rented to a local farmer and is a good source of income for Judy. She would like for her children to receive the rental income without the risk of the land being sold before her grandchildren can enjoy it.

This scenario is an example of a landowner who wants to dictate how the land is owned and managed after her death. While this may seem a bit harsh or controlling, it is completely within the legal rights of a landowner to control land after death. It is obviously important to Judy that the land stay in the family for at least two more generations. Judy is not providing discretion to her children to sell the land in order to accomplish this goal.

The concept of a trust holding farmland works well because the trust is the owner of the farmland, not the beneficiaries. The trust document, established by the grantor sometime before death, establishes the rules that carry out the grantor's goal of protecting the land from leaving the family. The trust document also designates a trustee who is tasked with carrying out the trust instructions. The trustee is obligated to manage the trust assets as directed by the trust document and is not beholden to the beneficiaries.

To illustrate this idea, let's continue the previous example.

Judy establishes a trust and transfers her land into the trust. While Judy is alive, she is the Trustee of the trust and can change the trust anytime she wishes. Essentially, the trust and Judy are the same person while she is alive. The trust is drafted so that when Judy dies, her son Kyle becomes the Trustee. The trust contains the following provisions for the land:

> *"My farmland shall be held in trust for the lives of my children. While my children are living, they shall receive all net income from the land in equal shares. While the land is held in trust, my Trustee may not sell, transfer, convey or encumber the land. Upon the death of the last of my children, the farmland shall be transferred to my then living grandchildren in equal shares."*

By using a trust, Judy can ensure that her children will get the benefit of the land without the being exposed to the risk of the children selling the land. The children will receive the income from the land but not have the ability to sell the land. Judy can be sure that her land will be inherited by her grandchildren in the future.

Trusts can also hold land for a shorter period of time while certain conditions are met. It is not uncommon for farmland to be held in trust for five or ten years so that the heirs, especially heirs not familiar with the farmland, have a chance to enjoy ownership before they may be tempted to sell the land. Also, the land may be kept in trust for younger heirs so that they have time to gain some maturity before becoming owners of the land.

Consider the following example.

Don owns family farmland and his children, Fred and Emily, will inherit the land. Fred and Emily have never been involved in the farm or farmland. They have said they may want to sell the land because they are not sure how to manage it. Don thinks they would be better off owning the land and getting a steady stream of rental income the rest of their lives, but he does not want to tie up the land forever. Don establishes a trust and requires the land be held in the trust for five years before being distributed to Fred and Emily. During the five years, a family friend familiar with managing farmland will be the trustee. The friend will help Fred and Emily with managing the land in the hopes of Fred and Emily wanting to keep the land instead of selling it when they receive it out of trust after five years.

Trusts are an effective tool at keeping farmland in the family. By taking advantage of the flexibility and creativity in planning that trusts provide, the current owner of the land can control how the land is used and who inherits the land in the future. Although trusts are not for everyone, landowners should consider incorporating a trust into their plan to help protect the land for future generations.

Limited Liability Companies

A well-designed LLC can make it very difficult for land to leave the family involuntarily. An LLC can protect land from partition, creditors and even divorces. However, the LLC can also be designed to allow the family to make joint decisions as to how to manage the land and sell the land. Provided the family members who own the LLC agree, they can lease, mortgage or sell the land. The LLC ensures that any transfer of land will only occur as a result of a family decision, and no one owner can force the sale of the land.

Consider the following example.

Linda, Mike, and Nancy own farmland together that they inherited from their parents. They agree they want the farmland to stay in the family for future generations, but they do not want to make it impossible for future owners to sell the land if the right opportunity presents itself. They decide to establish an LLC for the farmland. The terms of the LLC require a two-thirds consenting vote of the Members to sell or transfer the farmland.

Linda, Mike and Nancy can be sure that the land will not be transferred outside of the family unless ta majority of the family decides, as a group, to take such action. They can also be assured that if future generations decide it is best to sell the land and can gain a two-thirds vote, that opportunity will be available.

An LLC is created by state law and is registered with the secretary of state. After forming the LLC, an operating agreement is drafted which establishes the rules, terms and conditions for the LLC and its members. Then, the land is transferred to the LLC by deed. Only after the land is transferred to the LLC is it protected by the LLC.

An important characteristic of an LLC is that it is not subject to partition. As discussed above, partition rights are available to co-owners of real estate. When an LLC holds real estate, the LLC is the legal owner of the property. An owner of the LLC owns the LLC but does not own the land. So, co-owners of an LLC do not have partition rights on the land. This is why LLCs are valuable for protecting family farmland.

Operating agreements. The operating agreement is the key to an LLC's ability to keep land in the family. This document should outline the following terms, all of which are important to protecting the farmland:

- Who are permitted owners of the LLC?
- What happens in the event of an attempted ownership transfer outside the family?
- What percentage of ownership or owners is required for the transfer of land?
- What percentage of ownership or owners is required to amend the operating agreement?
- Can a member voluntarily withdraw?
- What percentage of ownership or owners is required to dissolve the LLC?

Each of the above terms should be carefully considered and discussed among the members establishing the LLC. Not only should the original members consider how the operating agreement terms will affect themselves but also how the terms will affect future generations of owners. In fact, the operating agreement is often more important to future generations that it is to the establishing generation. The following explains two important considerations for the members establishing the operating agreement—permitted owners and attempted transfers outside the family.

Permitted owners. Perhaps the first issue to consider when establishing a land LLC is permitted ownership. The operating agreement should clearly define who may become an owner in the LLC. The permitted owner definition can be very narrow or quite broad, depending on the goals of the LLC. Generally, the broader the definition the more risk of a transfer outside the family. A permitted owner can become a member of the LLC at any time without consent from the other members.

The hardest decision with defining the permitted owners of an LLC may be what to do about spouses of the owners. On the one hand, an owner may want their surviving spouse to have adequate income for the remainder of their life if the owner passes away. Therefore, it may be appealing to permit a surviving spouse to become an owner of the LLC. On the other hand, a surviving spouse can remarry while they are an owner of an LLC. Remarriage creates the risk of family LLC ownership being transferred, intentionally or unintentionally, to a surviving spouse owner's new spouse. The new spouse is unlikely to be related to the family members that own the LLC, creating a risk that the new spouse will transfer ownership to other non-family members.

Consider the following example.

Linda, Mike, and Nancy establish LMN Family Farms LLC to hold their family farmland. The operating agreement allows Linda, Mike and Nancy's spouses to be permitted owners of the LLC. Linda passes away and her share of the LLC goes to Oscar, her husband. Oscar later marries Patricia. Oscar never bothers to implement a proper estate plan and has a simple will leaving all his assets to Patricia. Oscar dies and Patricia claims that his ownership transferred to her and that she is now an owner of LMN Family Farms LLC.

Mike and Nancy are now left with having to deal with Patricia, a person who has no ties to their family and whom they may not even know. Additionally, Patricia may have no appreciation or sentimentality with the family farm and may see this as an opportunity for a payout. While Patricia may not be able to force the sale of the land or have voting rights, she will likely be entitled to a share of the LLC profits. [13] That is, a share of the profits are lost to someone who has no connection to the family.

Conversely, if LMN Family Farms had prevented spouses from being owners in the LLC, Linda's share may never have gone to Oscar. Perhaps, instead, Linda set up a trust to hold her LLC ownership for Oscar's life so he could receive the income for his life. Then, at Oscar's death, the ownership would transfer to Linda's children. Or Linda's ownership may have gone directly to her children at death.

[13] A person who receives an ownership interest in an LLC and who is not a permitted owner nor admitted by the other members is an Assignee. An Assignee is generally limited to an economic interest (profits) but does not have voting or management rights.

The point of the previous example is to closely analyze the implications of allowing spouses to be owners in a family-held LLC. There are advantages and disadvantages to including spouses as permitted owners. Allowing spouses to be owners can help provide for them upon the death of the LLC owner. However, allowing spouses to be owners can allow ownership to be transferred outside the family.

The purpose of many land LLCs is to pass the ownership from one generation to the next. Therefore, children and other lineal descendants are usually included as permitted owners in a family land LLC. This allows the ownership to pass down through generations.

Using the same scenario as above, assume the LMN Family Farms LLC operating agreement allows only lineal descendants to be permitted owners. Linda's estate plan leaves her LLC ownership interest to her children. When Linda dies, her ownership will be inherited, without the consent of Mike and Nancy, by her children. Linda's children will become full owners with voting and management rights. Linda's children will be able to transfer their shares to their children, and so on. Ownership can be transferred through generations indefinitely.

"A poorly drafted operating agreement or one that is not reflective of the family's goals can cause farmland to leave the family."

Trusts and estates may also be permitted owners. An LLC owner can direct their ownership interest to be held in a trust that is set up for a spouse or children. Also, an estate may be a permitted owner, which would allow a member's ownership interest to be transferred to other permitted owners via their estate. Without including trusts and estates as permitted owners, upon the death of an owner their ownership interest may not be transferable to their spouse or heirs.

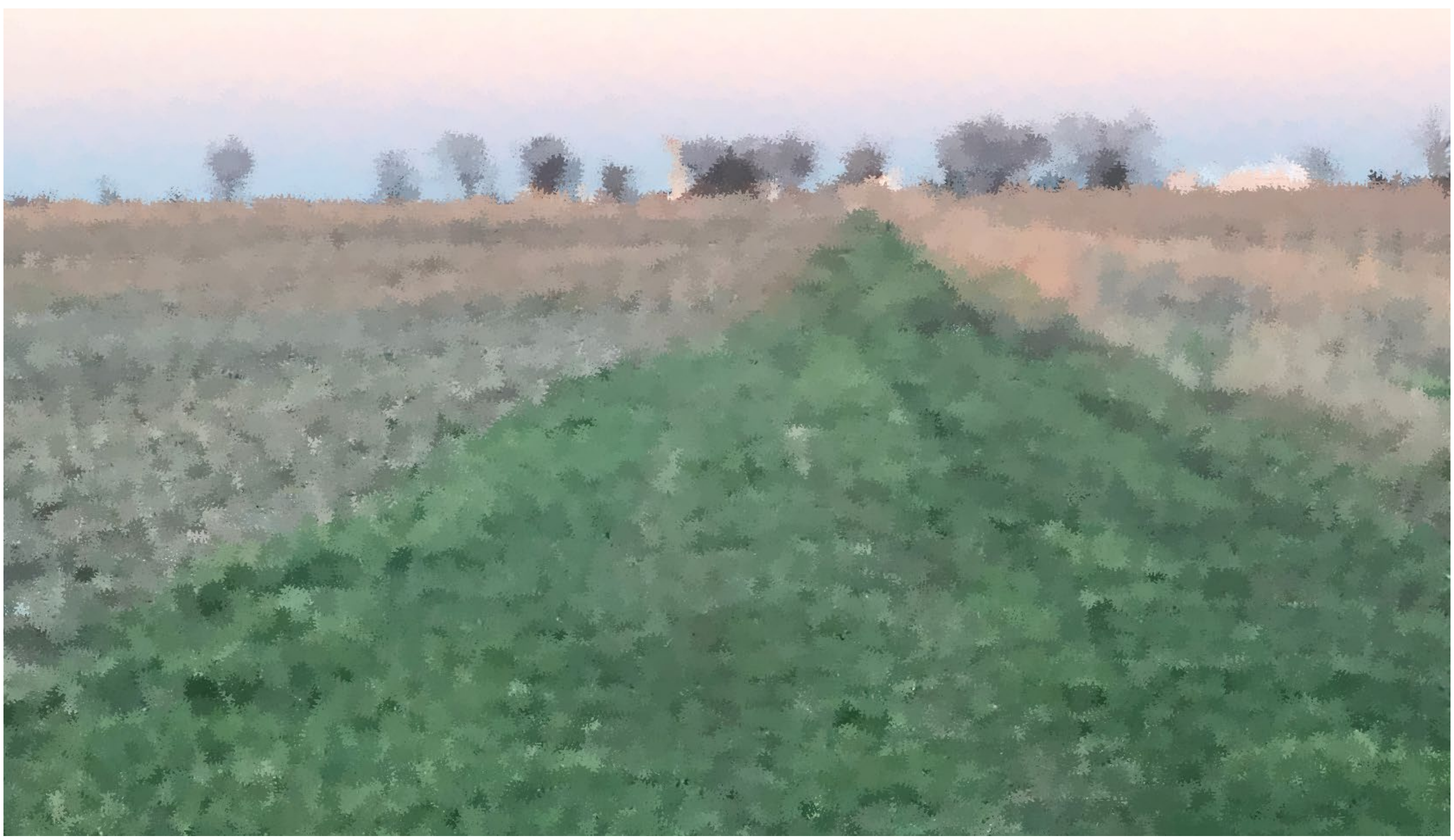
As the above discussion shows, establishing the class of permitted owners is an important part of establishing a family farmland LLC. The family should work closely with an attorney familiar with family farm issues to ensure the operating agreement matches their goals and objectives for the family farmland. A poorly drafted operating agreement or one that is not reflective of the family's goals can cause farmland to leave the family.

Attempted transfer of LLC ownership outside of family. Sometimes there can be an attempt to transfer LLC ownership outside of the designated permitted owners or family. Such a transfer can be voluntary, but it is usually involuntary due to divorce, death, creditors, or a legal judgment. The LLC operating agreement should address the possibility of an ownership transfer outside of the family. A transfer receiver who is not permitted to be an owner in the operating agreement will likely only be an assignee with limited rights.[14] But a provision in the LLC can allow the ownership rights to instead be bought back by the permitted family owners.

A "buy-back" provision states that either the LLC or other LLC members have the right to buy back someone's ownership before it would be transferred to a non-permitted owner. The LLC or other members would have the option to purchase the ownership before it is transferred to a non-permitted owner or could allow the ownership to transfer if they don't want to purchase it. This provision can help ensure that ownership, as well as all income from the LLC, remains in the family.

Consider the following example.

Linda, Mike, and Nancy are members of LMN Family Farms LLC. The LLC operating agreement states that the only permitted owners are Linda, Mike, Nancy, and their lineal descendants. A buy-back provision also states that other members of the LLC can buy another member's ownership interest before it is to be transferred to a non-permitted owner. Linda dies and her husband Oscar inherits her assets, including her LLC ownership. Mike and Nancy decide to purchase Linda's ownership interest. Oscar will receive the sale proceeds and Linda and Mike will now be the sole owners of the LLC.



[14] An assignee is someone who has received an ownership interest in an LLC but is not permitted to be a member and/or has not been voted in as a member of the LLC. Assignees have no voting or management rights.

As this example shows, a buy-back provision allows the family to keep control of ownership. Even though Oscar would be an assignee who is only entitled to an economic interest in the LLC, it is often better to purchase the ownership so that the family retains full control of the LLC and its economic interests.

The LLC operating agreement can also include favorable purchase terms for a buy-back. One term often included is a discount on the purchase price. The discount allows the other family members or LLC to buy back the transferring ownership at less than fair market value. The discount can be small or as much as 35-40%, depending on the situation. The discount gives an incentive to the other family members to purchase the ownership rather than have it held by a non-family member.

Another term that may be included in a buy-back provision is a payment term that would allow the purchase price to be paid over several years. Reducing the need to come up with a lump sum purchase price can help the other LLC members be able to buy the ownership interest. When the purchase price is relatively large, the LLC or family members may not have the funds available or be able to obtain a loan to make the purchase. Like the discount on purchase price, extending the payment schedule is likely to help keep ownership in the family.

Consider the following example.

Using the previous example, assume Linda's share of the LLC is valued at $1 million before discount. The LMN Family Farms LLC operating agreement states that a discount of 25% will be included in any purchases triggered by a transfer to a non-permitted owner. Additionally, the buyer(s) may pay the purchase price over 10 years at the minimum IRS allowable interest rate. Instead of Mike and Nancy having to pay $1 million to Oscar up front, they can pay him $750,000 over 10 years. Between the discount and the payment term, Mike and Nancy are much more likely to be able to buy-back Oscar's share into the family.

As these examples demonstrate, a well-designed LLC can make it difficult for farmland to leave the family. Because LLCs take away partition rights, a family decision is required for any action regarding the land. Ownership of the LLC can be restricted to family members and their lineal descendants. Buy-back provisions can further ensure that ownership of the LLC doesn't transfer outside of the family. For landowners who anticipate their land being owned by multiple family members in the future, including an LLC into their succession plan can be a useful tool for keeping the land in the family.

Rights of First Refusal

Sometimes the right estate planning strategy for a family can be for each beneficiary to receive a specific farm or parcel of land. This type of plan is often a good strategy when the current owner of the land does not want the land to be owned jointly by the future owners and also does not want to tie the land up in a trust. In situations such as these, a Right of First Refusal (ROFR) can be used to help keep the land in the family.

A ROFR requires an owner of land to enter into a sales agreement with a designated person before anyone else if the land is to be sold. In the context of family-owned farmland, a ROFR requires one family member to offer to sell to another family member before attempting to sell the land outside of the family. The ROFR can include many different terms and conditions and a landowner should include many details to avoid confusion or disputes related to the purchase rights. The most important details to address include purchase price, timeline, exempt transfers, and term of the ROFR.

Purchase price. The purchase price of the land is the most important term in a ROFR. One way to establish the purchase price is by matching a bona fide offer. Upon receiving an offer to purchase the land, the owner must offer to sell the land at that same price to the holder of the ROFR. If the holder declines to purchase the land at that price, the owner is free to sell to the third party at that price.

Another way to establish the purchase price is by appraisal. If the appraisal method is used, a multi-step approach should be considered to avoid the effect of an outlier appraisal. For example, the owner can obtain an appraisal first and if the buyer objects to the owner's appraisal, the buyer can obtain another appraisal. If the two appraisals do not match or are not within a certain percentage of difference, the owner and buyer would agree to have a third appraisal. After the third appraisal is conducted, the middle appraisal of the three establishes the purchase price. Also, the ROFR could include any qualifications for appraisers such as licensing or not being affiliated with the parties. This method is used when there is no offer to establish a price but the owner wishes to sell the property.

An ROFR could contain both an offer matching and an appraisal method for determining the purchase price. Terms could state that the price will be the lesser of an offer and an appraisal. The important point is to make it very clear how the purchase price is established and avoid disputes between the owner and potential buyer.

Timeline. Timelines in a ROFR ensure that the parties understand deadlines and keep the transaction moving. The following timelines are important for an ROFR:

- Number of days to provide an offer to the ROFR holder.
- Number of days to establish the purchase price by appraisal.
- Number of days to accept or reject an offer by the ROFR holder.
- Number of days to close the purchase.

Exempt transfers. Another term to consider is transfers that will be exempt from the ROFR. The owner may want to be able to transfer the land to a family member or spouse without triggering the ROFR. Therefore, the ROFR should specifically state all exempt land transfers.

Consider the following example. Tom agrees to give Susan a ROFR on land he owns. The ROFR expressly exempts any transfers to Tom's children. Tom later dies and his son, Ron, inherits the land. Susan's right to buy the land under the ROFR is not triggered because a transfer to children is exempt from the ROFR. If son Ron later attempts to sell the property, Susan's rights under the ROFR apply. The only exempt transfer is to Tom's children and all other transfers will trigger the ROFR.

Term. The length of term of the ROFR is also an important provision. Causing future owners of land to be subject to a ROFR indefinitely can cause problems if the rights under the ROFR pass to future generations. The landowner may have to track down many successors to the ROFR before being able to sell the land. Limiting the term of the ROFR to a certain number of years or to specific generations can avoid this problem.

Consider the following example.

In 1980, Joe granted a ROFR to Keith. The ROFR says it is binding upon their "heirs, assigns and successors." Joe and Keith have both passed away. Larry, Joe's son, inherited the land from his father and now wants to sell it. Because the ROFR from 1980 never terminated, Larry must find all of Keith's heirs and have them release their ROFR interest or exercise their right to purchase. Larry has difficulties finding all of Keith's heirs as they are scattered across the country.

This scenario shows the problems of having an indefinite term for the ROFR. If Joe and Keith would have made the ROFR effective for their lives only or for a certain number of years, Larry would not have to track down all of Keith's heirs, who may not have any connection to or interest in the land.

"A Right of First Refusal is relatively easy to implement and allows the landowner to still have the ability to sell the land."

ROFRs in estate plans. An ROFR can be coordinated with an estate plan and set up through a trust. It is common for a trust to include a provision that land being distributed to a beneficiary is subject to a ROFR in favor of another family member. The trust or will creating the ROFR should include the terms and conditions of the ROFR. The more detail provided, the less likelihood of future conflict among beneficiaries.

Consider the following example.

Henry owns two farms, Blackacre and Greenacre. Henry doesn't think his two children should own assets together because they don't get along well. He doesn't want to tie the land up in a trust and wants his children to have significant control over their land. His preference is for the land to stay in the family but that is not an absolute restriction he wants to place on the land.

Henry establishes a trust that gives Blackacre to son Isaac and Greenacre to daughter Jane. The trust also states that before distributing the land the Trustee is to execute a ROFR for each farm with the following terms:

- Before selling the farms, each child must offer the other child a chance to purchase.
- Purchase price is the lesser of a bona fide offer and an appraisal.
- The appraisal must use the three-step appraisal method.
- The purchase price is to have a 10% discount and can be paid over 10 years.
- Once the price is established, the child has 30 days to decide to purchase the farm and an additional 60 days to close the sale.

- Transfers to Henry's descendants and spouses of children are exempt from the ROFR.
- The term of the ROFR is only for as long as Isaac and Jane are alive.

When Henry dies, Isaac and Jane will each receive their specific farm subject to the ROFR. If either wants to sell during their lifetime, they must offer the farm to their sibling. The ROFR gives the other sibling a chance to buy the farm before it is sold outside of the family. The ROFR doesn't guarantee the land will stay in the family after Henry's death but it does at least allow a family member a chance to buy the land and keep it in the family.

ROFRs do not provide the same level of protection for farmland that trusts and LLCs provide. However, when heirs will own land individually, and not jointly, a ROFR will at least give other family members the right to buy the land before it could leave the family. A ROFR is relatively easy to implement and allows the landowner to retain the ability to sell the land, providing a moderate level of protection for keeping the land in the family.

Leases

Leases are also a tool that can keep land in the family. Like ROFRs, leases do not provide the same protection as LLCs and trusts but they can help. Leases can secure the land base for a farming heir by requiring non-farm heirs to lease their land to the farming heir. Typically, these types of leases are long-term, sometimes as long as 30 or 40 years. Note that in Ohio, a lease for more than three years must be notarized and should be recorded.[15]

Leases can be set up during life or at death through a trust. A trust can include a leasing provision requiring the non-farm heir to lease their land back to the farming heir and receive the rental income. A lease can also be used for land held in an LLC by off-farm heirs.

Consider the following example.

Keith and Lisa own two farms and want Mary to inherit Blackacre and Nancy to inherit Greenacre. Mary will continue the farming operation after Keith and Lisa's deaths, but Nancy is not involved in the farming operation. Keith and Lisa's trust includes the following provision:

> *"Our trust shall distribute Greenacre to Nancy. However, prior to distribution, the Trustee shall offer to cash lease Greenacre to Mary for 20 years provided Mary is farming. The lease rate shall be the county average and all other terms shall be at the discretion of the Trustee and Mary."*

In this example, Nancy will inherit Greenacre and will own it outright. However, she must offer to lease it back to Mary for 20 years. Keith and Lisa's plan makes sure that Nancy will inherit the farm but also will protect Mary's land base for her farm operation.

While a long-term lease can protect the land base for a farming heir, leases can significantly impede an owner's ability to sell the land. That is, land subject to a long-term lease may be difficult, if not impossible, to sell because a

[15] A short-form memorandum of lease may be recorded rather than the actual lease. ORC 5301.251

written, recorded lease is binding on the next owner. In the above example, Nancy may have a difficult time finding a buyer for Greenacre while Mary's lease is in effect. So, while Nancy will own Greenacre, she is severely restricted in how she can use it. If Nancy was expecting to cash out and receive money from the sale of Greenacre, she will be disappointed with the long-term lease requirement. This negative impact should be taken into account when considering long-term leases.

If a plan does use a long-term lease, a lease rate adjustment mechanism should be included in the terms of the lease. A 20-year lease with no allowance for a rental rate adjustment may become unfair to either the owner or tenant by the end of the term. Requiring the new owner and the tenant to negotiate a new lease rate every few years can address this problem. If the owner and tenant are unable to negotiate a new lease rate, the lease can include a means to determine the new lease rate.

One way to determine the rental rate is to use university or government lease data for the state or county. This method has a potential weakness, as the county and state averages may not accurately reflect the rental rate for a specific farm. For example, a farm may have much better soil and productivity characteristics than the average farm in the county. Another way to determine the new lease rate is the use of a third-party. An appraiser or other person familiar with farmland rent in the area can establish a farm market lease rate for the farm at issue. The third-party should be agreed upon by the owner and tenant. The disadvantages to this method are the potential for the two parties to be unable to agree upon a third-party and the third-party may expect to be paid for their services. Regardless of the method used, it is important that long-term leases have a solution for resolving lease rate adjustments.

Leases can be valuable tools to allow non-farm heirs to own farmland while protecting the farmland base for the farming heirs. The terms of the lease should be carefully considered to be sure the leases will be effective and meet the goals of the current owners. Both the benefits to the farming heir and the disadvantages to the non-farm heir owning the land should be considered when considering a long-term lease.

Agricultural or conservation easements

Placing a conservation or agricultural easement on land can ensure that the land will remain in agricultural or conservation use in the future. An easement strategy involves voluntarily agreeing to use the land only for agriculture or conservation and forfeiting the right to develop the land for other purposes. A legal deed of easement on the land documents the agreement to restrict the land use to agricultural or conservation purposes and gives the "holder" of the easement the right to enforce its provisions. The holder is typically a land trust or a government agency.

Beyond ensuring that the land will remain in agricultural or conservation use in the future, there are also financial incentives for entering into an agricultural or conservation easement that can help keep the land in the family. Through the Office of Farmland Preservation's Local Agricultural Easement Purchase Program, the Ohio Department of Agriculture uses Clean Ohio bond revenues and federal funds to pay landowners who qualify for the program and agree to place agricultural easements on their land.[16] A qualifying landowner is paid part of the development value of the land and must also "donate" a portion of that value. Land trusts and local governments hold the easements and may also have federal and private funds for easement purchases. Selection for easement purchase programs can be competitive.

Landowners may also "donate" an agricultural or conservation easement without receiving any payment. In either a donated or purchased easement situation, federal income tax benefits are available for the value of the portion of the easement a landowner donates. [17]

Easements that receive payment or federal income tax credits are intended to be permanent and the landowner seeking an easement should assume as much. An easement will prevent any residential or commercial development on the property. Improvements and land use activities on the land may or may not be allowed and will depend upon the specific terms of the easement. Also, many easements prohibit the land that is subject to the easement from being subdivided into smaller parcels. Due to the inability to develop the land or divide the land, the market value of the land can reduce but it likely holds greater appeal as agricultural land because it is protected from development.

Selling an agricultural easement allows a landowner to tap into the land's equity and use the proceeds to pay debt, purchase additional land, or address other risks to the land. Additionally, it may be less appealing to sell the land out of the family because the land can't be developed and future owners must use the land only for agricultural or conservation purposes in perpetuity.

Consider the following example.

John and Sue are fourth generation owners of 300 acres of farmland that they plan to leave to their son Lee, and they want it to remain as farmland. Lee is committed to farming and wants to farm, but John and Sue would like Lee to have more land and improve the viability of his operation. They apply to Ohio's Local Agricultural Easement Purchase Program and are selected for the program. They receive a payment of $2,000 per acre for entering into an agricultural easement that protects the land permanently as agricultural land. They use the $600,000 in easement proceeds to purchase additional farmland for Lee and apply for a federal income tax credit for the portion of the easement value they donated to qualify for the program.

[16] https://agri.ohio.gov/programs/farmland-preservation-office

[17] Internal Revenue Code §170(h).

This example illustrates how landowners who are comfortable placing a permanent easement restriction on their land can use the agricultural easement strategy. The strategy can protect the land and provide financial benefits that can help ensure the land will remain in the family as part of a viable farming operation.

Combining strategies

The strategies discussed above are not exclusive and can be combined to serve the needs of a farm family. For example, perhaps a family uses an LLC in combination with a long-term lease. Or a family could place an agricultural easement on land that goes into a trust. All strategies should be considered, as well as the possibility of using a combination of strategies to carry out the goal of keeping the farmland in the family.

Summary

Real threats exist that can cause farmland to leave the family. When landowners want to reduce those threats, there are several tools that can help protect the farmland. The level of protection can vary from near absolute, like a trust, to merely giving other family members a first chance to buy the land, like a ROFR. The level of protection and the methods to enforce this protection are key decisions in keeping farmland in the family.

Finding legal and professional assistance

The need for legal counsel in providing guidance for the best strategy to protect farmland is critical. There is likely a solution that meets the goals of the current landowners and experienced legal counsel can help find that solution.

Farmers can find attorneys familiar with keeping farmland in the family in a number of ways. Often the best way is through referrals from friends and family. Another way to find an attorney is to contact the local or state bar associations and agricultural Extension Educators. If a referral is not available, a simple internet search can be effective. Searches for "agricultural estate planning," "farm estate planning," and "agricultural attorneys" will often identify attorneys that may be able to assist with planning strategies.

Whatever the method to search for an attorney, be sure the attorney has experience dealing with farmland and farming operations. Family farms have unique issues that an attorney unfamiliar with farming may not understand or recognize. Using an experienced agricultural attorney to implement a strategy is the final step toward keeping farmland in the family

This is a project of the **OSU Agricultural & Resource Law Program**, an OSU Extension program providing objective and timely legal research on agricultural issues affecting Ohio. Find other law bulletins in this series and all our resources on OSU's Farm Office website, a one-stop shop for agricultural law and farm management information.

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Long-Term Care and the Farm

An examination of long-term care needs, risks, and strategies for protecting farm assets

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Extension

National Agricultural Law Center

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Long-Term Care and the Farm

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EXTENSION

Using this information

This publication aims to provide a basic explanation of Long-Term Care (LTC) issues and strategies that may minimize exposure to LTC risks. **The publication is not a substitute for professional legal advice.** Presenting every law and exception related to LTC planning is beyond the scope of this material, but the guide introduces concepts and strategies that can help a farmer begin a detailed discussion with professional advisors. LTC planning can be technical and complicated and should occur in conjunction with a careful review of an individual's situation. Before taking any actions on LTC, consult with an attorney and other professional advisors experienced in LTC issues.

This publication is based on **Ohio** laws and regulations. Each state has its own Medicaid rules, and other laws may vary from state to state. While strategies addressed in this publication may generally apply across all states, it is imperative to understand the laws and Medicaid regulations of the state of residence before taking any LTC planning actions.

Thank you to our reviewers

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1. The Risk of Long-Term Care

Family farms are unique from other types of businesses in that a family farm is not just a business. The family farm is also a way of life and a celebration of family heritage. For most farm families, a primary goal of estate and succession planning is continuing that family farm legacy for future generations.

In the past, perhaps the biggest threat to the continuation of family farms was estate taxes. In 2002, the exemption from federal estate taxes was only $1 million per person and the tax rate on estate assets over the exemption was 50%. Many states also had estate taxes. Due to the relatively low estate tax exemptions and high tax rates, even moderately sized farms faced significant estate tax risk. If cash was not available, farm assets, including farmland, were often sold to pay estate taxes.

The estate tax environment is very different today. In 2022, the federal estate tax exemption is $12.06 million with an estate tax rate of 40%.[1] According to the Congressional Budget Office, only about 0.2% of estates pay estate taxes. So, estate taxes are no longer the primary threat to farmers who want to leave their farms to future generations.

Instead, the biggest financial threat to continuing the farm today is likely Long-Term Care (LTC) costs. Many farm families may struggle to pay LTC costs for the older generation. When cash or insurance runs out, farm assets may have to be sold to pay for the care. As our population continues to age and care costs continue to increase, the problem is not likely to go away. In fact, the financial

[1] The current estate tax exemption is scheduled to revert to 2017 levels ($5.49 million plus indexing for inflation) after 2025.

pressure of LTC costs on family farm succession will probably increase.

This publication takes a closer look at how LTC might affect the future of farms. It examines the potential risk of needing LTC and statistics that help predict the expected costs of LTC. It also presents strategies that can help mitigate LTC threats to the farm. The intent is to provide a general understanding of the issues of LTC so that farmers can make informed decisions about how to plan for LTC.

This area of the law is fraught with exceptions as well as technical and nuanced rules and regulations. It is not possible to address every scenario for every farm family. Therefore, farm families should only implement LTC strategies after careful consultation with legal counsel and other professional advisors.

What is long-term care?

The Administration for Community Living defines LTC as:

> *Services that include medical and non-medical care for people with a chronic illness or disability. LTC helps meet health or personal needs. Most LTC services assist people with Activities of Daily Living, such as dressing, bathing, and using the bathroom. LTC can be provided at home, in the community, or in a facility. For purposes of Medicaid eligibility and payment, LTC services are those provided to an individual who requires a level of care equivalent to that received in a nursing facility.* [2]

As the definition indicates, LTC can mean different types of services for different types of needs. On one end of the spectrum, LTC may be occasional, in-home personal care assistance. On the other end, LTC may be a nursing home providing skilled services. The type of LTC greatly affects the costs of the services. The most common types of LTC are home-base care and facility-based care.

Home-based care

Most LTC is home-based, providing care that allows a person to remain at home.[3] Unpaid family members and friends are typical providers but paid caregivers may be involved. A range of services such as the following are available for home-based care.

Home health care involves part-time medical services ordered by a physician for nursing care or assistance after surgery, an accident, or an illness. It may include physical, occupational, or speech therapy services.

> *"The biggest threat to continuing the farm today is likely long-term care costs… the financial pressure of LTC costs on family farm succession will probably increase."*

[2]https://acl.gov. The Administration for Community Living is within the U.S. Department of Health and Human Services. Its mission is to maximize the independence, well-being, and health of older adults, people with disabilities across the lifespan, and their families and caregivers.

[3] National Institute on Aging, https://www.nia.nih.gov/health/what-long-term-care

Homemaker and personal care services assist individuals at home with meals, household chores, and personal care needs.

Friendly visitor and companion services are typically volunteers who regularly pay short social visits to an individual in their home.

Transportation services help people with shopping, medical appointments, and similar transportation needs.

Emergency medical response systems summon emergency medical assistance via an alert system like a necklace or remote. These systems usually involve a monthly fee.

Facility-based care

If adequate care cannot be provided at home, a person might require care from an LTC facility. The services range according to need.[4]

Independent living apartments are ideal for those who want social interaction and planned events but don't need personal or medical care. These facilities do not require licensing or governmental oversight.

Adult homes are licensed to provide short or long-term residence in a small setting and usually include supervision, personal care, housekeeping, and three meals a day.

Enriched housing is also licensed like adult homes, but residents live in independent housing units.

Family-type homes are licensed and offer long-term residential care for up to four adults who are not related to the operator.

Assisted living programs are an alternative to nursing homes for those who need daily help but not 24-hour care.

Continuing care or lifecare communities have a variety of facilities on one campus to allow "aging in place" for a resident to move from one level of care to the next as needs change. They usually require an up-front purchase price and ongoing monthly payments.

Nursing homes and skilled care facilities offer 24-hour-a-day care by staff and trained medical professionals, with daily care and medical services for those who can no longer live independently or are suffering from on-going health and recovery issues.

What do statistics say about long-term care risk?

There is no doubt that LTC costs are a financial threat to many farms. Some farmers may go to great lengths to protect their farm assets from potential LTC costs by gifting assets to family members, transferring farm assets to irrevocable trusts, or buying LTC insurance. But when is it necessary to take such actions, and what might be the **actual risk** that LTC costs will affect a farmer and farm assets?

Statistics can help us better understand potential LTC needs. The following data presents the type of LTC required for a typical person over the age of 65, the average length

[4] University of Rochester Medical Center, https://www.urmc.rochester.edu/senior-health/long-term-care/facility-types.aspx

of time a person will require each type of LTC, and the average costs of LTC services.

Data on length and type of LTC

A person turning age 65 today has a 69% chance of needing some type of LTC services in their remaining years, according to the Administration for Community Living.[5] On the other hand, 31% of those over 65 will not require LTC.

On average, 3 years of care will be needed. Due to women having longer life expectancies, women will require an average of 3.7 years of care and men on average will need 2.2 years of LTC. Some people will require a longer period of care, however. Twenty percent of adults will need LTC care for longer than 5 years.

Table 1 summarizes the current data on the length of care someone 65-years or older may need in the future, and the expected type of care that will fulfill their care needs. The table shows that of the 3 years of LTC a person will need on average, 2 of those years would be provided at home. A majority of LTC services are reportedly given at home because people do not want to leave home and go to a facility. Only 1 year of the average 3 years of care needed would be provided in a facility.

Additionally, a portion of at-home care needs are met through unpaid care provided by family or friends. When there is a cost for home-based care, the cost is typically less expensive than facility-based care. A person might expect that all LTC will be provided in a facility, but as **Table 1** shows, most care is the home-based care.

Table 1. Expected type and length of LTC services

Type of LTC	Years needed	% who will need it
Any LTC services	3	69
Home-based care		
Any services	2	65
Unpaid	1	59
Paid	<1	42
Facility-based care		
Any services	1	37
Nursing home	1	35
Assisted living	<1	13

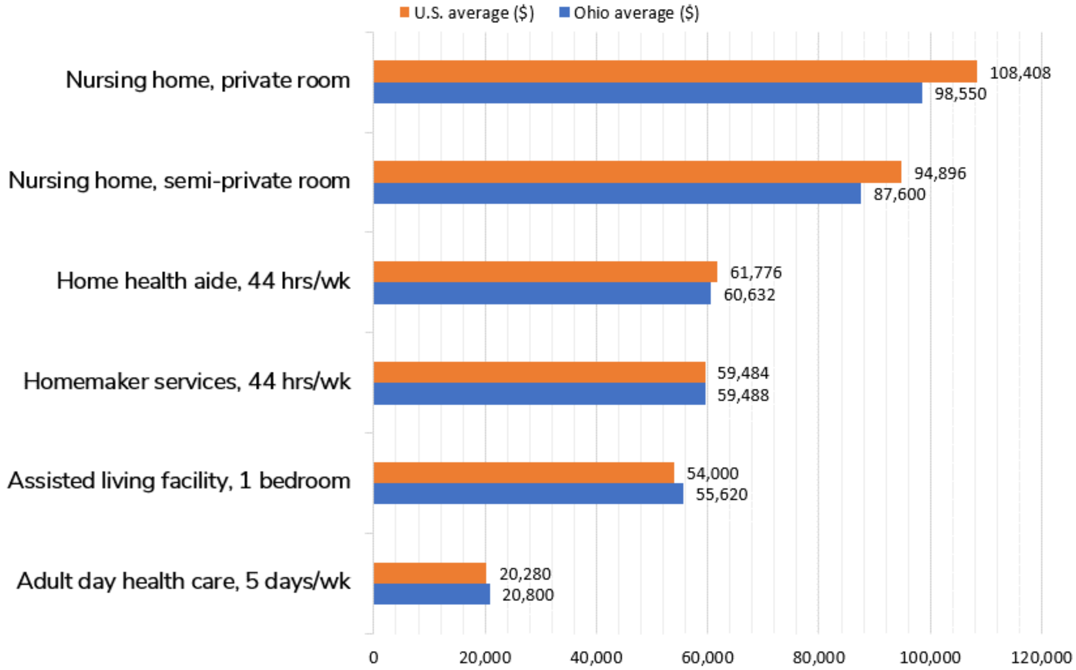
Average costs of LTC

The next important statistic that can help us understand LTC risk is average LTC costs. **Table 2** on the following page shows the average costs of different LTC services according to the *2021 Cost of Care Survey* provided by Genworth Financial, Inc.[6] The table presents both Ohio and national averages. The data illustrates that facility-based costs are significantly higher than home-based care services and that in 2021, the average cost of a year of nursing home care in Ohio was nearly $100,000.

[5] Administration for Community Living, https://acl.gov/ltc/basic-needs/how-much-care-will-you-need.

[6] https://www.genworth.com/aging-and-you/finances/cost-of-care.html

Table 2. Average costs of LTC services



Let's use the data above to make predictions for an average Ohio farmer. Table 3 provides LTC assumptions based on the statistics and shows that a 65-year-old Ohio farmer can expect about $150,000 in LTC costs.

Table 3. Estimated LTC needs for a 65-year-old farmer

Chance of needing LTC	69%
Expected length of LTC	3 years
One year of unpaid home-based care	$0
One year of paid home-based care	$60,000
One year of facility-based care	$90,000
Total cost of 3 years of LTC	$150,000
Chance of more than 5 years of LTC needed	20%

Covering LTC Costs

The next question is, can the average farm absorb the potential cost of LTC without jeopardizing farm assets? Keep in mind that these costs are per person and a married farm couple will have double these potential costs. How could a farm family pay for LTC costs? Annual income, non-farm assets, and farm assets may be available to cover LTC costs.

Annual income. First, we must consider that a farm family could have annual income to use for LTC costs. Farm income, land rent, social security income, and income from investments could all be available to pay for LTC costs.

Non-farm assets. After using annual income to pay for LTC care costs, non-farm assets like savings may be available to pay for the costs.

Farm assets. It's the portion of the LTC costs that income and savings cannot cover that causes farm assets to be at risk. For example, if a farmer has $100,000 in savings, that savings will not cover all potential LTC costs of $150,000, leaving farm assets at risk for the remaining unpaid balance of $50,000.

While a farmer would probably not want to sell any farm asset to pay for LTC, their land is probably the last asset they would want to sell. Most farmers may prefer to sell grain, crops, livestock, and machinery before selling the farmland. But if income and savings cannot pay for LTC care costs, how at risk is the farmland asset?

Data can help us answer the land risk question. According to the Economic Research Service at USDA (ERS), the total *non-real estate* equity owned by farmers in the U.S. for 2020 was $533.7 billion. The ERS further estimates that there were 2.02 million farmers in the U.S. in 2020. On average, farmers owned $188,654 of non-real estate equity. This suggests that if income and savings cannot pay for LTC costs, the average farmer would have an additional $188,654 of assets to sell before needing to sell real estate.

The risk of being an outlier

So, what does LTC data tell us? The average farmer, if forced to sell farm assets to pay for LTC, will probably not need to sell the land. An average farmer may need to sell crops, livestock, or machinery to pay for LTC costs but the land is probably safe. That is the good news.

The bad news is that the data analysis is based on averages. When dealing with large numbers, averages are very useful. We can say with some confidence that on average, a 65-year-old farmer in Ohio will pay between $0 and $150,000 for LTC costs. However, the numbers cannot tell us with certainty what a specific person will spend on LTC. Farmer Smith in Delaware County, Ohio might never have any LTC costs, or may pay the average of $150,000, or might be an outlier.

An outlier is one whose specific circumstances are significantly different than the average. Being an outlier is the risk any farmer faces with LTC. We all know someone, or have heard of someone, who was in a nursing home for 10 years. That's close to $1 million in LTC costs for that outlier. Few farmers have the income, savings, and non-real estate assets to pay for $1 million of LTC if they end up in an outlier situation.

What LTC planning for most farmers really equates to is protecting against the outlier scenario that puts the land at risk. Most 65-year-old farmers would probably sleep well at night if they knew they would have no more than $150,000 of LTC costs for the rest of their lives. That amount of LTC costs is probably not going to cause a farm liquidation. What may keep farmers up at night, including the young next generation farmer, is the worry that they or their parents will be the outliers who will spend 10 years in a nursing home.

The outlier scenario is important to keep in mind as farmers develop an LTC strategy. For any risk management plan, the true nature of the risk must be understood and not just presumed. The facts show that most farms can probably withstand average LTC costs. It is also factual that most farms cannot withstand an outlier scenario that requires many years of LTC care. This understanding is critical to developing a LTC plan.

The LTC Contract

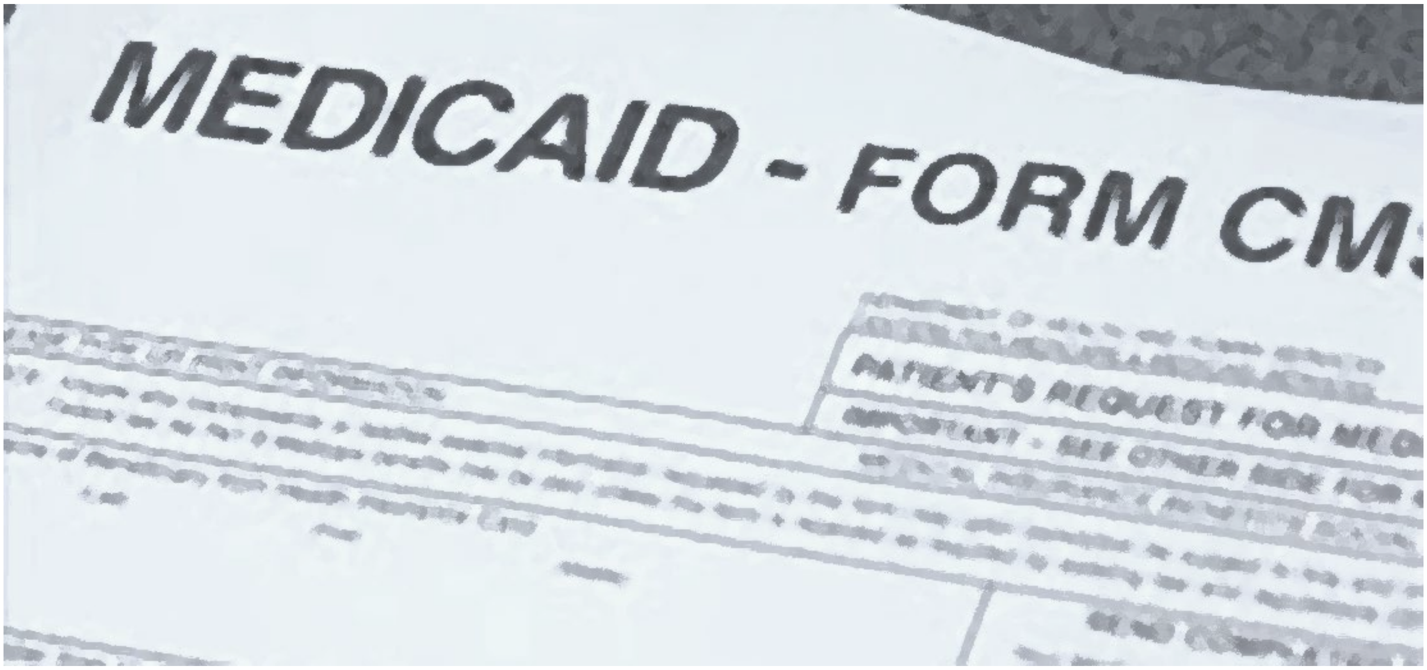
LTC providers typically use contracts to document and enforce payments for LTC services. The contract will likely outline the consequences of not paying the provider for their services, such as an end to the services or a requirement to move out of the facility. If a person's financial assets are exhausted, an LTC contract might state that the person must apply to Medicaid for payment.

Any money owed to a service provider in a contractual situation can be collected through litigation. The LTC provider can file a lawsuit against the client and foreclose on their assets. Also, the LTC contract will likely require the client to pay for the nursing home's collection fees, including attorney fees.

Paying an LTC provider is not optional. A service provider is not under an obligation to continue to provide services if not being paid. The point here is that if money runs out and an LTC client owns assets, those assets must be sold to create funds to pay for the care.

Consider the following example.

Farmer Smith signed a contract with the nursing home facility he has been in for one year. He has used up his savings and other funds to pay for the first year of care. If Farmer Smith cannot pay for the cost of continuing his care, the facility can refuse further services and force him to leave the facility. Farmer Smith owns $200,000 of machinery and $1 million of land. He may have to sell his assets to pay for continued LTC care. If he decides to sell his machinery, the sale proceeds must be used to pay for his care as agreed to in the LTC contract. If he exhausts those funds and is still in the facility, he will likely have to sell his land to pay for his care.



2. Assistance from Government Programs

Government programs can provide financial assistance towards LTC costs. The two programs most commonly associated with LTC are Medicare and Medicaid. While the programs may sound similar in name, their impact on LTC costs is very different. The following explains each program and their effects and limitations on LTC.

Medicare and LTC

Medicare is federal health insurance for anyone age 65 and older, and for people under 65 with certain disabilities or conditions. Medicare may provide some short-term coverage of facility-based care costs. If the stay in a nursing home requires skilled services for a medical condition that is hospital-related, Medicare will pay 100% of the nursing home costs for the first 20 days and a portion of the costs for days 21 to 100. After 100 days, Medicare will not pay for LTC costs.

In general, Medicare will pay for short-term nursing home costs if the stay is related to recovering from a stay in a hospital. Medicare will not pay for LTC if the care is only for Activities of Daily Living, such as dressing, bathing, and using the bathroom. Medicare may be used by people receiving LTC services to pay for prescription drugs and physician services. Due to the limited amount of time that Medicare will pay for LTC services, Medicare should not be considered a viable strategy for LTC cost coverage.

Medicaid and LTC

Medicaid is a joint federal and state program that provides health coverage for people with limited income and resources. Medicaid offers benefits such as nursing home care, personal care services, and assistance paying for Medicare premiums and other costs. Funds for Medicaid come from both federal and state governments. The federal government sets certain minimum standards but gives the states flexibility on the services they provide. This is especially true for home care.

Federal law requires states to provide Medicaid coverage to low-income families, low-income pregnant women and children, adults over the age of 65, and people with disabilities. Each state has the option to expand Medicaid coverage to include other groups. For example, some states also cover low-income adults. It is important to know the specific eligibility requirements of the state in which the Medicaid application is made.

Medicaid covers many different types of medical needs for many different people. However, the remainder of this publication focuses on the application of Medicaid in relation to LTC costs.

Medicaid eligibility

Medicaid is available only to those who meet its eligibility criteria, explained below.

Residency. An applicant for Medicaid must be a United States citizen and a resident of the state in which application is made.

Age or disability. The applicant must be either 65 years old, blind, or disabled. People under age 65 who may qualify based on a disability include adults and children with disabilities they have had since birth and others who have disabling conditions acquired through illness, injury, or trauma. Medicaid beneficiaries enrolled through disability include those with physical conditions such as quadriplegia or traumatic brain injuries; intellectual or developmental disabilities such as cerebral palsy, autism, or Down syndrome; and serious behavioral disorders or mental illness such as schizophrenia or bipolar disorder. [7]

Income limits. Some people may be ineligible for Medicaid if their income is too high. Medicaid analysis includes all income sources for the applicant and some of a spouse's income. Table 4 below lists monthly income limits for Ohio Medicaid eligibility in 2022.

Table 4. Ohio monthly income limits for Medicaid eligibility

Marital status	Limit ($)
Single	2,523
Married, one spouse applying	2,523
Married, both spouses applying	5,046

While Medicaid does have income limits, being over the limit has a solution. A person with income exceeding the limit can establish a

[7] Medicaid and CHIP Payment and Access Commission (MACPAC). https://www.macpac.gov.

Qualified Income Trust (QIT). If the individual transfers all gross income exceeding the limit into the QIT, the individual can be within the Medicaid income limit. The QIT income can be used to pay for small personal needs, Medicare premiums and medical costs not covered by Medicare. All remaining funds must be used to pay for LTC costs.

It is important to note that a QIT does not protect the excess income from LTC facility costs. The excess income will still need to be used to pay for LTC care costs. The QIT simply prevents the individual from needing to claim the income, thus allowing eligibility.

Consider the following example

Ellen is not married and receives $3,000 per month in income. Her monthly income exceeds the Medicaid limit. She establishes a QIT and transfers her $1,000 social security check to the QIT each month.

Ellen now has $2,000 per month in income and qualifies for Medicaid. She pays $200 per month for Medicare premiums and $50 for personal needs. The remaining $750 per month in the QIT goes to pay for Ellen's LTC costs.

Asset limits. Generally, a person may own only very limited assets if they are to qualify for Medicaid. The idea behind this is that if a person owns assets, they should use those assets to pay for the LTC rather than having Medicaid pay. The asset limitation is usually the biggest impediment to farmers qualifying for Medicaid. Due to the capital-intensive nature of farming, farmers often own too many assets to be eligible for Medicaid without aggressive planning.

Each state identifies the maximum value of *countable* assets that a person can own and qualify for Medicaid but note that some assets are not countable and are exempt from the Medicaid asset limits, explained in the next section.

Table 5 shows the asset limits for Ohio in 2022.[8]A single person may not own more than $2,000 of *countable* assets to qualify Medicaid. A married couple can own no more $3,000 if they are both to be eligible for Medicaid. For a married couple with only one spouse attempting to be eligible for Medicaid, the applying spouse may own not more than $2,000 of countable assets and the non-applying spouse may own $137,400.[9]

Table 5. Ohio asset limits for Medicaid eligibility

Marital status	Limit ($)
Single	2,000
Married, one spouse applying	3,000
Married, both spouses applying	2,000 applicant + 137,400 non-applicant

Due to the Medicaid asset limits, a single farmer must own almost no farm assets to be

[8] American Council on Aging, https://www.medicaidplanningassistance.org/medicaid-eligibility-ohio/.

[9] The amount of assets that may be owned by each spouse depends on which assets are owned by each spouse, how the assets are owned and the type of asset. This analysis can be complicated and is beyond the scope of this publication.

eligible for Medicaid. A married couple may be able to own a few acres of farmland but little else. These extremely low eligibility limits make it very difficult for farmers to qualify for Medicaid.

Assets exempt from Medicaid eligibility

Not all assets that a person owns is counted towards Medicaid eligibility. Some assets that are necessary to live or of a personal nature are exempt and not counted towards the $2,000/$3,000 asset limit. It is important to note, and as will be discussed later, that an exempt asset is still subject to Medicaid estate recovery. An exempt asset is temporarily exempt from being spent down but is still at risk to LTC costs. The following can be exempt assets.

Home. Generally, the home is not an exempt asset unless the person intends to return to their home after their LTC stay or if a spouse or dependent is living in the home. Medicaid exempts homes in these circumstances so that a person who is only in LTC temporarily has a home to return to and to not cause spouses and independents to lose their homes. If one of these circumstances is not met, the home is a countable asset and must be sold before gaining Medicaid eligibility. The home may not have equity of more than $636,000.[10]

It is important to note that Medicaid defines a home as including "land appertaining to the home property."[11] Therefore, farmland that is adjacent to the home can also be an exempt asset. However, a significant number of acres included with the home can cause the home to exceed the equity limit.

For married couples, it is very important to consider transferring the home to the spouse who will continue living in the home. The benefits may include increased protections for heirs and protection from estate recovery. Be sure to seek advice from an attorney regarding ownership of the home among spouses.

Consider the following examples.

Example 1. Jane is not married and owns a home on a 50-acre parcel valued at $400,000. Jane enters a nursing home but fully intends to return to her home after a temporary stay in a nursing home. Jane signs an affidavit stating her intention to return to her home. The home and 80 acres will be an exempt asset and not counted towards Jane's $2,000 asset limit.

Example 2. Same facts as Example 1 except Jane has serious physical restrictions and will never return to her home. The home with 50 acres is a countable asset and must be sold and the proceeds used to pay Jane's LTC costs before she can be eligible for Medicaid.

[10] Ohio Adm. Code 5160:1-06-02.1
[11] Ohio Adm. Code 5160:1-3-05.13 "Home", for the purpose of this rule, means any property in which an individual has an ownership interest in and which serves as the individual's principal place of residence. Home includes the structures and land appertaining to the home property. Appertaining land must adjoin the land on which the home property is located and must not be separated by intervening land property owned by others.

Example 3. Jane is married to Joe. Jane goes to a nursing home and will not return to her home. Joe continues to live in their home. The home and 50 acres will be an exempt asset for as long as Joe is residing there. If the home is transferred to Joe, and Joe must sell the home later, Joe is able to retain 100% of the sale proceeds. Joe should also have his estate planning documents carefully reviewed if he dies before Jane. The value of the home will not be counted towards Jane's $2,000 nor Joe's $137,400 asset limit.

Example 4. Same facts as Example 3 except Joe will no longer live in the home. Because neither Jane nor Joe will live in the home, the home and 80 acres are countable assets and will have to be sold. However, Joe has three months to purchase a replacement home.[12]

Household goods. The Ohio Administrative Code defines household goods as all personal property customarily found in or near the home and used on a regular basis in connection with the maintenance, use and occupancy of the premises. This encompasses items necessary for an adequate standard of sustenance, accommodation, comfort, information and entertainment of occupants and guests. Such items include furniture, household appliances, carpets, dishes, cooking and eating utensils, televisions, and personal computers.[13]

Automobile. One automobile may be exempt as long as it is used for transportation purposes.[14]

Cash value of life insurance. The cash value of life insurance is exempt provided the face value of all policies on the individual's life is less than or equal to $1,500. If cash value exceeds $1,500, the policies must be cashed out and proceeds used to pay for LTC costs.[15]

Burial plot and prepaid funeral expenses. A burial plot for the individual and immediate family members are exempt assets.[16] Prepaid funeral expenses up to $1,500 are also an exempt asset.[17]

Retirement accounts. Some, but not all, retirement accounts are exempt assets.[18] The determination depends on the type of account, status of current payouts, requirements for taking payments and amount of the payments. There is no simple rule or formula to determine the exemption status of retirement accounts; there must be a thorough analysis by someone familiar with Medicaid rules for each account. Countable retirement accounts must be cashed out and the proceeds used to pay LTC costs. All income from exempt retirement accounts must be used to pay for the LTC costs.

Property used in a trade or business. While someone receiving LTC is unlikely to be operating a farm, the spouse may continue farming. The land, machinery and livestock can be exempt as property used in a trade or business. Merely renting farmland is not

[12] Ohio Adm. Code 5160:1-3-05.16
[13] Ohio Adm. Code 5160:1-3-05.10
[14] Ohio Adm. Code 5160:1-3-05.11
[15] Ohio Adm. Code 5160:1-3-05.12
[16] Ohio Adm. Code 5160:1-3-05.11
[17] Ohio Adm. Code 5160:1-3-05.6
[18] Ohio Adm. Code 5160:1-3-03.10

considered a trade or business. A Schedule F or similar tax filing must show earned income from the trade or business.

Consider the following example.

Jane is seeking eligibility for Medicaid. Her husband Joe owns 200 acres of land worth $2 million and $500,000 of farm machinery. Joe uses the land and machinery to conduct his farming operation.

The land and machinery would likely be considered exempt assets because they are used in the farm business. If Jane owns less than $2,000 of countable assets and Joe owns less than $137,400 of other countable assets, Jane can qualify for Medicaid.

Medicaid estate recovery

Assets that are exempt from being counted for Medicaid eligibility are not necessarily safe from LTC costs, as discussed above. After a person on Medicaid dies, exempt assets become subject to Medicaid payments. This process is called estate recovery. Essentially, Medicaid agrees to allow some assets to be exempt while a person is alive and receiving LTC. However, once the person dies, Medicaid rules expect the exempt assets to be used to reimburse for LTC costs paid.

Medicaid will delay estate recovery if either a spouse or child under 21 years old survives the deceased. However, Medicaid may recover the assets upon the death of the surviving spouse or the child reaching 21 years old.[19] Medicaid monitors those who are receiving benefits and upon learning of a recipient's death will take steps to ensure that estate recovery occurs.

Consider the following example.

Jane has been in the nursing home for two years and Medicaid has paid $100,000 for her care. Husband Joe has lived in their jointly owned home while Jane has been in the nursing home. After Jane's death, Joe continues to live in the home.

Upon Joe's death, Medicaid can take a lien on Jane's one-half share of the house, up to $100,000. Medicaid must receive $100,000 from sale proceeds from the house or the person receiving the home must pay the estate recovery. If the home was owned solely by Joe prior to Jane's death, Medicaid estate recovery would not apply.

Improper transfers and the five-year look-back period

A person may own only a limited amount of assets to qualify for Medicaid. The logical next thought is for the Medicaid applicant to simply divest themselves of their assets to attain Medicaid eligibility. However, Medicaid rules do not allow a Medicaid applicant to give away their assets one day and become eligible for Medicaid the next day. Becoming eligible for Medicaid by giving away assets is not an easy nor quick process.

In the application process, Medicaid looks back five years for any improper transfers. The five years is measured from the baseline date,

[19] Ohio Revised Code 5162.21

which is the first date the individual applies for Medicaid and is institutionalized.[20] All transfers during the "look-back period" are analyzed to determine if any transfers were improper. Any transfers prior to the look-back period do not affect Medicaid eligibility.

An improper transfer is a transfer of an asset for less than fair market value during the look-back period[21]. Fair market value means, unless otherwise stated, the going price, at the time of the transfer or contract of sale, for which real or personal property can reasonably be expected to sell on the open market in the relevant geographic area. The appraised value of real property determined by the county auditor and may be used to establish fair market value of real estate.[22]

There are a limited number of exemptions for improper transfers. These include a transfer of a residence to a spouse, a child under the age of 21, a child who is blind or disabled,[23] or to an adult child who has resided in the residence for at least two years and is providing care to the parent.[24]

Upon determining that an improper transfer occurred during the look-back period, Medicaid calculates the penalty period and the applicant is ineligible for Medicaid payments during that period. The penalty period is based on the value of the improper transfer divided by the Average Private Pay Rate (APPR), currently $6,905.[25] This number, rounded to the next full number, is the number of months the person is ineligible for Medicaid payments. The penalty period technically has no limit. However, if the application for Medicaid is not made until the look-back period has expired, the penalty period is essentially capped at the 60-month look-back period.

Consider the following examples.

Example 1. Arthur makes an improper transfer of $100,000 to his children. The $100,000 gift divided by the APPR of $6,905 equals 14.5, and Arthur will be ineligible for Medicaid coverage for 15 months.

Example 2. Arthur makes an improper transfer of $1 million to his children. The $1 million gift divided by the APPR of $6,905 equals 144.8. This gift would make Arthur ineligible for Medicaid payments for 145 months. However, Arthur waits 60 months after the gift to apply for Medicaid. Because the five-year look-back period has passed, the $1 million gift is no longer an improper transfer and does not cause a penalty for Arthur.

The examples show that as long as a person waits to apply for Medicaid after the look-back period ends, the look-back acts as a 60-month cap on the improper transfer penalty period. This makes LTC planning very difficult, as it must occur five years in advance. No one knows what their physical condition will be in five years. Therefore, LTC planning often involves best guesses and risk management rather than certainties and qualitative decisions.

[20] Ohio Adm. Code 5160:1-6-01.1
[21] Ohio Adm. Code 5160:1-6-01.1
[22] Ohio Adm. Code 5160:1-1-01(B)(27)
[23] Ohio Adm. Code 5160:1-6-06(D)(1)
[24] Ohio Adm. Code 5160:1-6-06(D)(2)
[25] Ohio Department of Medicaid

Improper transfers and no money to pay for LTC

What happens if a person gifts away their assets to qualify for Medicaid but then goes into a facility such as a nursing home before the look-back penalty period has lapsed? If the gifts are returned to that person, the penalty period will be withdrawn and the returned assets would have to be spent down or used for payment of the LTC costs. After the assets have been exhausted, the person can be eligible for Medicaid. Another option is for a person who received a gift to retain the gift and pay for the LTC costs until the look-back penalty period has lapsed.

Undue hardship exemptions

It is possible to request an undue hardship exemption. An undue hardship can occur if the imposition of the penalty period deprives an individual of:

1. Medical care, such that the health or life of an institutionalized individual would be endangered, or
2. Food, clothing, shelter, or other necessities of life.[26]

There are several requirements for obtaining an undue hardship exemption:[27]

1. An undue hardship exists;
2. The institutionalized individual currently has no alternative income or resources available to provide the medical care or food, clothing, shelter, or other life necessities the individual would be deprived of due to the imposition of the penalty period; and
3. A good faith effort to pursue all reasonable means to recover the transferred asset or the fair market value of the transferred asset was made, or documentation shows that the cost of any such effort would exceed the gross value of the assets subject to recovery. These good faith efforts may include:
    a. Seeking the advice of an attorney and pursuing legal or equitable remedies such as asset freezing, assignment, or injunction; or seeking modification, avoidance, or nullification of a court order, financial instrument, promissory note, loan, mortgage or other property agreement, or other similar transfer agreement;
    b. Cooperating with any attempt to recover the transferred asset or the fair market value of the transferred asset.

If a person is in a LTC facility, there are two additional conditions for successfully making an undue hardship claim:

1. The care facility has planned to discharge the institutionalized individual as a result of the imposition of the penalty period; and
2. The institutionalized individual has exhausted all administrative remedies to challenge the planned discharge.

Medicaid typically closely scrutinizes hardships. Gifts should never be made in anticipation of later receiving an undue hardship. The persons receiving the gifts should be aware of the improper transfer rules

[26] Ohio Admin Code 5160:1-6-06.6(C)

[27] Ohio Admin Code 5160:1-6-06.6(E)

and the implications of the five-year lookback period.

Rental and care agreements

A rental or care agreement is a legitimate way to transfer money from a parent to a child for Medicaid purposes. Because rent and care payments are for a service, they are not considered an improper transfer of a gift. This means that a parent who lives with a child may pay the child rent and it will not be considered a gift.

A written rental agreement and/or care agreement can specify the details of the arrangement, such as the rental amount, the care to be provided, and the compensation for that care. The rent must be reasonable, based on the housing expenses of the child or the fair market rent for a similar residence. Likewise, the parent can compensate the child a reasonable amount for providing care to the parent. Payments for rent or care can expedite Medicaid qualification by transferring wealth away from the parent.

3. Strategies to Mitigate LTC Risk and Protect Farm Assets

There are strategies that can mitigate LTC risks to farm assets and help secure the farm for future generations. However, it is probably impossible to find a perfect strategy that completely protects all farm assets from LTC needs. Choosing and implementing a strategy can be technical, legal, and complicated, and will require the assistance of an attorney and other professional advisors. Acting without the advice of legal counsel could make an already challenging LTC situation even worse.

The following strategies can have significant risks or disadvantages. Carefully weighing the disadvantages against the advantages can help identify a strategy that will work best for an individual farm situation.

Do-nothing

When we hear of a “do-nothing” strategy, we might consider it the same as failing to have a strategy. However, with LTC, a do-nothing strategy might be the best strategy. It is most appropriate for those who have sufficient income for LTC and are willing to use that income to pay for LTC costs. No planning is necessary. Provided adequate income is available to cover even an outlier scenario, farm assets will not be at risk of being sold for LTC costs. When income is adequate, perhaps the best strategy is to do nothing other than pay the LTC costs and retain farm assets.

Consider the following example.

Tom and Sara have retired from farming. Between retirement accounts, investments, land rent, and payments for the sale of their machinery, they expect to have $300,000 of annual income available for the rest of their lives. They don't plan for LTC costs since their income should meet their needs.

Even if both Tom and Sara go into a nursing home for several years, which would be an outlier event, they should have enough income to cover all potential LTC costs. The risk that they will need to sell their remaining assets to pay for LTC costs is very low. Thus, a legitimate strategy for them is to keep their assets and rely on their income for LTC costs.

When considering the do-nothing strategy, be sure to take into consideration future increases of LTC costs. As previously shown in **Table 1,** LTC costs increase around 3-6% each year. Income that is adequate to pay for LTC today may not be adequate in the future.

Gifting assets

Gifting assets is a preferred LTC strategy for many people. The strategy is to give away assets and wait for the Medicaid improper transfer penalty period to lapse so that the gifted assets are safe from LTC costs. A gift must be a true gift and not illusory. That is, the gift must be made free of payment and conditions. The person making the gift cannot keep ownership and control of the asset.

There are several disadvantages of the gifting strategy. The first is potential ineligibility for Medicaid due to an improper transfer. As discussed previously, each $6,905 of value of a gift causes one month of ineligibility of Medicaid, up to the five-year maximum look-back period. To protect assets from LTC costs, the assets must be gifted five years before an application for Medicaid is filed.

A second disadvantage of gifting assets is losing the income from those assets. One does not receive income from assets they do not own. The same goes for assets they have gifted. The person who gifted the assets no longer owns them and should not expect to receive income from them.

A third disadvantage is the loss in stepped-up tax basis at death. A person who inherits assets receives the deceased person's stepped-up basis for the assets. The stepped-up basis allows a sale of the assets for no or little gain in basis or capital gains tax liability. All things being equal, it is much better to inherit assets with a stepped-up tax basis than to receive assets by gift with no stepped-up basis. Also, inherited business assets can be re-depreciated.

A final disadvantage is that gifts can use up the federal estate tax exemption. Gifts exceeding the $16,000[28] annual gifting exclusion will either cause a gift tax or a reduction in the unified credit for the federal estate tax exemption. It is usually more beneficial to choose to reduce the estate tax exemption than to pay gift tax. For example, a

[28] Annual gift exclusion for 2022 is $16,000 and $17,000 for 2023. The annual gift exclusion is indexed and is increased by $1,000 every few years.

$1.016 million gift will reduce the donor's federal estate tax exemption from $12.06 million to $11.06 million. See our law bulletin on *Gifting Assets Prior to Death* at farmoffice.osu.edu for a thorough discussion on the implications of gifting.

Consider the following example.

Janet owns 200 acres of land. She is concerned that if she goes into a nursing facility, she will have to sell the land to pay for her care. She purchased the land in 1980 for $1,000/acre. It is now worth $10,000/acre. Janet decides to gift the land to her son, Joe.

In this example, Janet gifted land valued at $2 million. To protect the gift, she must allow the five-year look-back period to expire before applying for Medicaid. Joe received the land with a $1,000/acre tax basis and will pay tax on the $9,000/acre gain if he sells the land. Also, Janet's unified credit will reduce from $12.06 million to $10.06 million.

If Janet had kept the land and Joe inherited the land at her death, he would receive the stepped-up $10,000/acre tax basis. If Joe sells the land for $10,000/acre, he will not pay tax on the sale because there is no gain.

When gifting assets, the advantage of protecting the assets must be weighed against losing the stepped-up basis at death. Losing the stepped-up basis can be a significant loss to the potential heir. It is quite possible that the risk of LTC costs to the assets will be outweighed by the stepped-up tax basis. For example, if the risk to the assets is relatively low and the financial gain of a stepped-up tax basis is high, it may be better to accept the risk of LTC costs to achieve the stepped-up basis gain at death.

Irrevocable trusts

Many people have the misperception that if they have a trust, their assets are protected from LTC costs. However, revocable trusts do not provide asset protection and are not an effective strategy for guarding assets from LTC costs. Most trusts are revocable trusts that can be changed or revoked at any time. The grantor or creator of the trust can transfer assets to and from the trust at any time. Just as the grantor can take assets out of a revocable trust, so can a creditor like an LTC facility.

However, an irrevocable trust can protect assets from LTC costs. This type of trust does not allow a grantor to withdraw assets once the trust is established and assets are transferred into it. The grantor cannot revoke the trust or regain control of the assets, one of the disadvantages of a revocable trust. The trustee appointed for the trust, who cannot be the grantor, has the sole authority to manage the trust assets. Because the grantor no longer owns or has control of the assets, the grantor's creditors, like an LTC facility, has no rights to the assets.

An irrevocable trust has an advantage over a gifting strategy because a grantor can still establish terms and conditions for what happens to the assets in a trust. For example, a grantor can put restrictions on selling farmland or require assets to be held in the trust for several generations.

An irrevocable trust can also be set up so that the grantor can retain some income from the trust, another advantage an irrevocable trust has over a gift. However, the income from the trust is not protected from LTC costs. A grantor must decide whether to keep income from an irrevocable trust when establishing the trust, as the income cannot later be "turned on" and "turned off" by the grantor as needed.

One disadvantage of an irrevocable trust is that for Medicaid purposes, a transfer of assets to the trust triggers the improper transfer penalty. Therefore, the grantor will not be eligible for Medicaid until the five-year look-back period passes.

Cost is also a disadvantage of an irrevocable trust. These trusts are complicated instruments that must be established by an attorney familiar with LTC and asset protection. Thus, legal fees can be significant with costs sometimes exceeding $10,000.

Another disadvantage of an irrevocable trust is the ongoing management requirements. An irrevocable trust that does not reserve the income to the grantor must file an annual income tax return, have its own bank account, and essentially operate like a business entity. Failure to operate the irrevocable trust properly can jeopardize the assets in the trust.

A final consideration for an irrevocable trust is the effect on the tax basis of the assets in the trust. Generally, assets in an irrevocable trust receive a stepped-up tax basis at death if the grantor retains income from the assets while living. If the grantor does not retain income rights, the assets do not receive a stepped-up basis at the grantor's death.

Consider the following example.

Bill owns 500 acres of farmland that he wants to protect from LTC costs. He has other sources of income and does need the income from the farmland. He establishes an irrevocable trust and transfers the 500 acres to the irrevocable trust. Bill names his daughter, Susan, as trustee of the trust. The trust states that the land shall be held in trust for Bill's life. may not be sold, and the trust income is to be distributed to his two children. Upon Bill's death, the land is to go to his two children. If a child predeceases Bill, the child's share will be distributed to their children provided they are 25 years old.

Bill's transfer of the land to the irrevocable trust will cause him to be ineligible for Medicaid for five years. After that time, the transfer is no longer an improper transfer and does not cause Medicaid ineligibility. Also, after the look-back period has passed, the land will be protected from LTC costs because Bill no longer owns the land.

Susan, as the trustee, must manage the trust and collect income from the land, pay all expenses, distribute net income to herself and her sibling, and file an annual income tax return. She must follow the conditions of the trust and cannot sell the land. Bill is assured that while he is alive, the land cannot be sold.

At Bill's death, the land will be distributed to his two children. Because Bill did not retain any income from the land, the children do not receive a stepped-up tax basis on the land.

Wait-and-see

Many farmers adopt a wait-and-see approach for LTC costs. The idea is to wait to see when and if LTC care is needed. At that point, if necessary, assets to be protected are gifted or transferred to an irrevocable trust. This strategy requires enough resources to cover LTC costs until the five-year look-back period ends, then all assets transferred at the beginning of the look-back period will be safe.

Consider the following example.

Joe has $50,000 of annual income and $400,000 of savings. His only other asset is his farmland. Joe is reluctant to gift his land to his children in case they have financial difficulties and are forced to sell the land. He is also reluctant to transfer his land to an irrevocable trust because he does not want to give up ownership and control of the land and incur the costs of a trust.

Joe decides to take the wait-and-see approach. If his health declines and he must go into a nursing facility, he has enough income and savings to cover the five-year look-back period. Prior to going into a facility, he will gift or transfer his land to an irrevocable trust and use his income and savings to pay LTC costs for five years. After five years, the land will be protected from LTC costs.

The advantage to this plan is that Joe maintains flexibility. If he never incurs LTC costs, or incurs a relatively small amount, he can retain ownership of the land for the rest of his life. His income and savings provide him the ability to wait-and-see what the best strategy will be to protect his land. This keeps Bill from gifting his land to protect from LTC costs if he never actually incurs any LTC costs.

The disadvantage to a wait-and-see strategy is that significant assets must be available to pay for five years of LTC care. For people who do not have the resources to cover five years of LTC costs, this strategy may not work. For people who want to protect all of their assets, including savings, this is not the best plan. But it may be a good strategy for those willing to allow some assets, like savings, to be at risk to LTC costs in exchange for keeping ownership and control of their most important asset, land.

LLCs

LLCs and other business entities can be incorporated into LTC plans. Simply transferring assets to an LLC does little for LTC planning but an LLC may help implement some of the strategies identified above. For example, instead of landowners gifting land to their children, perhaps they put the land in an LLC and gift the LLC to the children. Holding the jointly owned land in an LLC protects against partition and helps keep the land in the family. See our publication on *Keeping Farmland in the Family* on farmoffice.osu.edu for a thorough discussion of using LLCs to protect family farmland.

An LLC is also a good way to gift assets but maintain some control over them. For example, a parent could transfer land to an LLC and gift 99% of the ownership to the children, while keeping 1% ownership. The LLC could be designed so that unanimous consent is required to sell any land. The parent could therefore prevent a sale of land with their 1% ownership. If the parent incurs LTC costs and seeks to qualify for Medicaid, the LLC could require the children to buy the parent's 1% interest. This strategy allows 99% of the value of the land to be gifted but allows the parent to prevent from being sold without their consent.

LLCs are also a good way to consolidate assets prior to gifting. It may be easier to transfer all assets into an LLC and then gift LLC ownership. This may be especially useful for farming operations with equipment and livestock. Also, LLCs provide the opportunity to gift ownership a little at a time although this advantage may not work well for LTC planning due to the improper transfer penalty period.

Self-insure

Another strategy is to self-insure against the possibility of LTC by setting aside specific assets to use for LTC costs. Typical assets would be cash or financial investments but could also include any type of asset, such as land. As LTC costs arise, the designated assets are used to pay the costs.

Consider the following example.

Mike and Nadine own five farms. One farm, the Smith Farm, is farther away than the others, is a less productive farm, and only recently purchased. Mike and Nadine decide that if they need LTC and do not have the income or savings to cover the cost, they will sell the Smith Farm to pay for their care. Mike and Nadine let their family know of their plan so that everyone is aware that the Smith Farm is the LTC insurance plan.

Self-insuring can be an excellent LTC plan because the owners retain full control of their assets as well as full flexibility to change the plan at any time. It does not require legal fees, premium payments, or other administrative costs, unlike other strategies with fees or administrative costs.

A disadvantage of the self-insure strategy is the unknown of how much will be needed to cover LTC costs and what value of assets to designate for the costs. If enough is not set aside and the money or assets are exhausted, all other assets will be at risk for LTC costs.

A second disadvantage of self-insuring is that the strategy can create an "impoverished spouse" dilemma when a married couple has decided to self-insure. Due to not knowing how long LTC costs may last for a spouse that goes into LTC care, the spouse not in need of care may be reluctant to spend anything on themselves other than bare necessities. The spouse at home may choose to live an impoverished lifestyle for fear that the self-insurance assets won't be enough for the LTC care needed.

Consider the following example.

Mike and Nadine decide to self-insure and manage to set aside $300,000 of savings for LTC. Mike's health begins to fail and he is admitted to an LTC facility. Their annual income only covers $40,000 of the $100,000 nursing home bill so they begin to use their savings to cover the balance. Odds are that the $300,000 savings will be enough for the costs but Nadine is afraid they will run out of money. Nadine no longer spends money for travel, entertainment, or quality of life expenses for herself.

LTC insurance

LTC insurance policies cover some or all LTC costs for an individual. LTC insurance policies, in many ways, provide the most flexible LTC plan. If a policy can be obtained to cover all LTC costs or at least cover the deficiency that income does not cover, farm assets can be protected. Therefore, a person can keep their assets and continue to enjoy and use them for the remainder of their lives.

It should be worthwhile to at least explore incorporating a LTC insurance policy into a LTC plan before assuming that assets must be gifted or transferred to protect them. Many insurance agents and financial advisors can provide free estimates for policies without too much difficulty. They can also help with a risk assessment to determine what policy may be needed for an individual's given circumstance. Depending on the type of policy and robustness of coverage, LTC policies can be expensive. Not everyone will be able to fit LTC policy premiums into their budget. Also, not everyone is insurable. People with significant pre-existing health care issues may not be able to obtain a LTC policy.

There are many different types of policies and coverages available. For example, some coverages start soon after LTC is needed while some do not begin to pay right away, sometimes starting to pay as long as one year after LTC begins. Also, some policies are combined with a death benefit so the policy holder receives at least some benefit from the policy if it is not used for LTC. The following are some, but not all, of the terms and conditions to consider when exploring a LTC insurance policy.

Duration of benefits. Most policies cover at least one year and may cover up to five. Policies that cover more than five years are no longer available. Obviously, a longer-term policy is preferable but that must be balanced against the higher premiums.

Benefit triggers. The LTC policy pays out when certain triggers, or conditions, exist. Before paying out, most policies require the policy holder to need assistance with at least two of the following activities: bathing, dressing, toileting, eating, transferring and continence. Be sure to understand what conditions are required for payout to be triggered.

Waiting period. Policies include a waiting period before the insurance benefits will begin. The waiting period may be a few days or as long as one year. The policy holder must cover LTC costs until the waiting period ends. The longer the waiting period, the lower the policy premiums.

Daily benefit amount. A LTC policy states a daily benefit amount it will pay for LTC care. Some policies may pay 100% of the daily LTC costs. Other policies may only cover 50% of the LTC costs. The policy can be used to cover only that portion of LTC costs that income does not cover.

Inflation protection. Like any cost, LTC costs will increase over time. Some policies have inflation adjustment built in and automatically increase over time. Other policies offer the holder the ability to increase the coverage to keep up with inflation but this will also increase the premium. It is important to know what type of inflation adjustment provision is in a policy.

LTC insurance Partnership Policies

Most states, including Ohio, have a Partnership for Long-Term Care Insurance program. This program provides asset coverage equal to the benefits paid by a LTC insurance policy. For example, if $100,000 of LTC was paid by insurance, the insured is eligible to retain an additional $100,000 above the asset limits provided in **Table 4** above. If available, a Partnership Policy could affect the decision to obtain LTC insurance and could be an important part of an LTC plan.

Combining LTC strategies

The strategies discussed above are not exclusive. One or more strategies may need to be combined to serve the needs of a farm family. For example, perhaps some assets are gifted as one strategy and a second strategy of an LTC insurance policy is obtained to cover the five-year look-back period and protect the gifted assets. Or another approach could use an LLC in combination with an irrevocable trust. All strategies should be considered for an LTC plan, as well as the possibility of using a combination of strategies in the plan.

4. The LTC Risk Assessment

Now that LTC risk, costs, and mitigation strategies have been discussed, it is worthwhile to have a more comprehensive discussion on assessing individual LTC risks. Until a risk assessment is performed for an individual situation, it is nearly impossible to determine the best course of action for LTC management strategies.

The risk assessment looks at the potential costs of LTC and the ability of the farm to pay those costs. Paying for LTC is a function of available income, LTC insurance, and assets that can be liquidated to pay for LTC costs not covered by income. Generally, the assumption is that farmers will first use savings to pay LTC costs not covered by income and insurance, then non-real estate farm assets, and then finally, real estate. That is, the land is the last asset a farmer will typically want to use to pay for LTC costs.

The assessment process

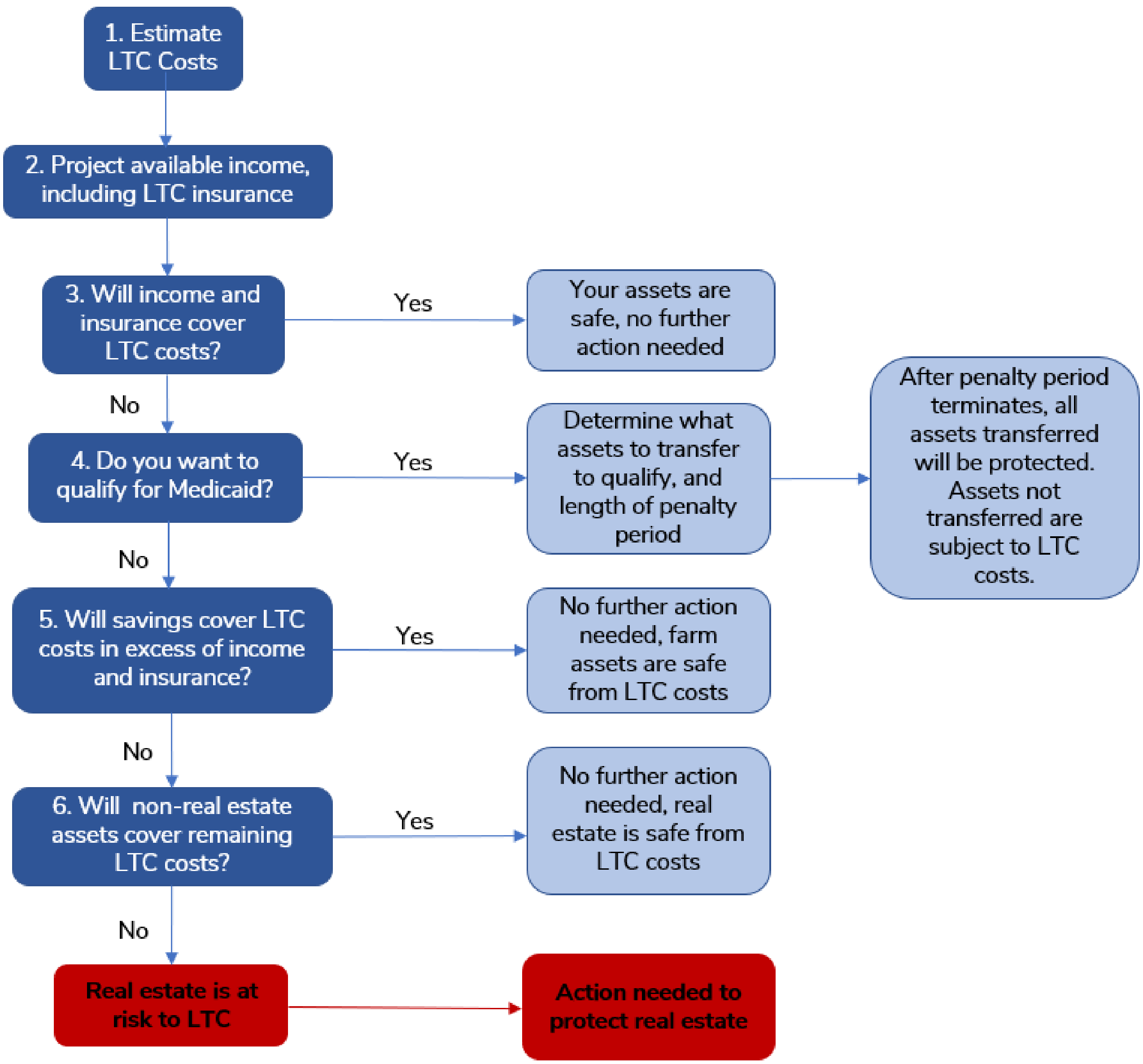
A step-by-step process can help an individual work through the LTC risk assessment. The steps below provide a guideline, as illustrated in **Figure 1** below.

1. Estimate LTC costs. To start an individual LTC assessment, make an estimation of what LTC costs might be. As discussed earlier, on average about 69% of people will need LTC and the average costs will be around $150,000. Also, recall that approximately 20% of people will be outliers and need LTC for more than five years, which could easily equate to $500,000 or more of LTC costs. There is no way to know exactly how much any one person will need for LTC costs but it is possible for an individual to decide whether to base planning on average LTC costs or an outlier scenario. As presented in Section 1, the

Genworth Financial Cost of Care Survey[29] is a good source for predicting current LTC costs.

2. Project available income. Forecasting a realistic income projection is next. It is important to keep in mind that if someone is receiving LTC, there is a good chance they will not be able to operate a farm. So, income should probably be based more on potential retirement income than income from an operating farm or wages. All available sources

Figure 1. Long-Term Care Strategy Analysis



[29] https://www.genworth.com/aging-and-you/finances/cost-of-care.html

of income should be included, such as retirement accounts, investments, land rents, and the sale of operating assets. The income forecast needs to be based on after-tax income. Also, factor in any LTC insurance benefits that may be available. LTC insurance payments can essentially be added to the income to help pay LTC costs.

3. Compare costs to income. The next step is to compare the income forecast, including LTC insurance, to potential LTC costs. If there is adequate income and insurance to pay for LTC costs, other assets are not at risk. Additionally, no further LTC planning likely needs done. Assets are only at risk to LTC when income is inadequate to cover the costs.

4. Consider Medicaid. If income and insurance will not cover the projected LTC costs, then a decision needs to be made regarding Medicaid. Is it a goal to qualify for Medicaid? If yes, what actions would need to be taken to qualify and what impact does the five-year penalty period have on the plan? Deciding if there will be reliance on Medicaid will dictate which of the LTC strategies are available and appropriate.

5. Assess savings. If Medicaid eligibility is not desired, then the next step is to determine how long savings will cover the deficiency. By dividing the available savings by the income deficiency, we can determine how many years of LTC will be covered by savings. If the savings will cover average LTC costs and outlier scenarios, then all remaining assets are likely protected.

Consider the following example.

Joe is an unmarried farmer with children. He has no LTC insurance. He forecasts his annual retirement income to be $50,000 after taxes. He has $500,000 in savings and investments, $500,000 in machinery and equipment and $2 million in land. He assumes that a nursing home will cost $100,000/year. His income is $50,000 short of covering the annual nursing home bill. If he uses his savings to cover the deficiency, he can pay for ten years of nursing home costs before his savings are depleted.

The average male will require about 2.2 years of LTC. Joe can pay for ten years, almost five times the average stay, with his income and savings. Joe's risk analysis shows that if he is willing to use his savings, his farm assets are at low risk of being consumed for LTC costs because it is unlikely Joe will need more than ten years of LTC.

6. Assess non-real estate assets. Many farms do not have much savings or investments because it is common for all money to be put back into the farm. In these situations, the question is whether and how much operating assets need to be liquidated to pay for LTC. Like the income forecast, available operating assets should be valued as after-tax.

Consider the following example.

Same example as above but Joe only has $50,000 in savings. In this scenario, his savings will only pay for one year of LTC. After that, he may need to sell machinery, which will pay for ten years of care.

In this risk analysis, Joe's savings and machinery are at risk to LTC costs. However, his land is likely safe unless Joe requires more than ten years of nursing home care, which is unlikely. But Joe may decide he is not willing to risk his machinery and instead transfer it to an irrevocable trust or elect another strategy to protect it from LTC costs. If he protects his machinery, he will also need to do the same for his land.

7. Address risk to land. If income, savings and operating assets are insufficient to cover LTC costs, then land is at risk. As stated above, this is almost always the asset most important to farmers and the asset requiring the most protection. If the risk analysis shows that the land is likely at risk to LTC costs, a farmer may need a strategy to protect the land, such as gifting to heirs or transferring to an irrevocable trust.

Consider the following example.

In Joe's example above, assume Joe had quit farming and does not own any machinery. Using his savings, he can only pay for one year of LTC before his land is at risk. Joe decides to gift his land to his children to avoid having to spend it down for LTC. Joe decided upon an aggressive LTC plan due to his land being exposed to significant risk from LTC.

Married couples require additional analysis. The examples above use a relatively simple scenario for a single person. For married couples, the assessment is more complicated due to the possibility of two people with LTC costs. Additionally, not all income can be allocated to LTC if one spouse remains at home with continuing needs. The risk assessment is more complex with marriage.

Until a risk assessment is performed, it is difficult to know what strategy to implement. When income and savings are adequate to cover many years of LTC, there may not be a need for aggressive LTC planning. If income and savings will only cover LTC for a short period of time, aggressive planning may be necessary to protect assets.

Finding legal and professional assistance

An attorney familiar with LTC issues can be helpful with conducting a risk assessment. Before transferring assets or implementing the plan, an attorney should be consulted. LTC planning can be complicated and technical. Implementing the wrong plan can make things even worse. A small investment in legal fees is worthwhile to be sure your LTC plan is the correct plan for your farm.

Farmers can find attorneys familiar with LTC in a number of ways. Often the best way is through referrals from friends and family. If a referral is not available, a simple internet search can be effective. Searches for "Elder Law Attorney," "Medicaid Attorney," and "Long-Term Care Attorney" will often result in attorneys that may be able to assist in LTC matters. Another way to find an attorney is to contact the local or state bar association and ask for a list of attorneys who practice in LTC matters. Whatever the method, be sure the attorney you select is familiar with and has experience in LTC matters.

In addition to finding an attorney who understands LTC, farmers should use an attorney who is also familiar with farm issues. The farm attorney might also have the LTC expertise or may collaborate with the LTC attorney. Family farms have unique issues that an attorney not familiar with farming may not understand or be aware of. For example, transferring an operating farm into an irrevocable trust may not a good strategy for a farm. To find attorneys familiar with farm issues, referrals from fellow farmers can be a good place to start. Also, a local Extension educator or farm organization representative often know attorneys who work with farmers.