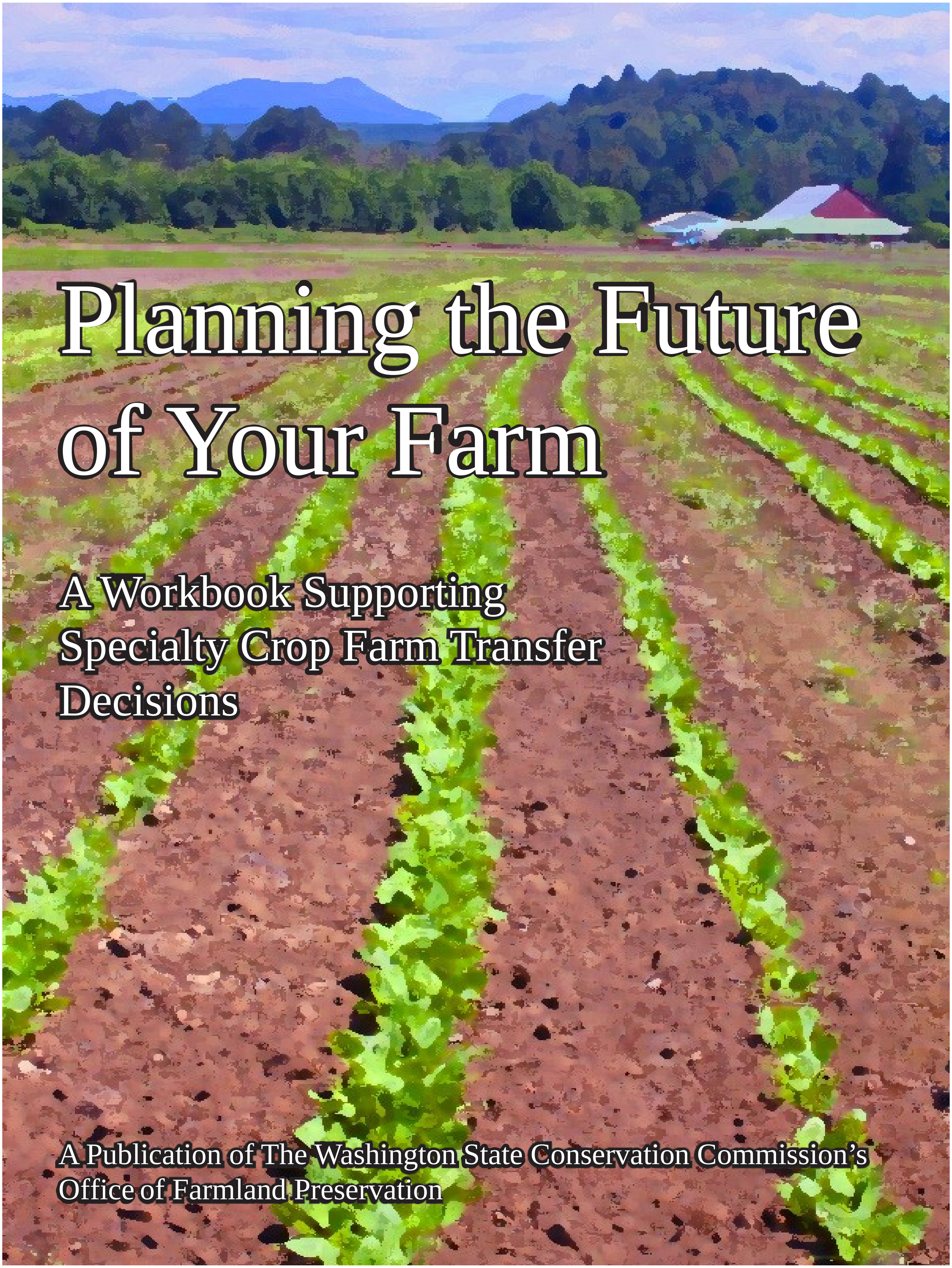

Planning the Future of Your Farm

A Workbook Supporting Specialty Crop Farm Transfer Decisions

A Publication of The Washington State Conservation Commission's
Office of Farmland Preservation

Acknowledgements

Thank you to all the specialty crop producers who continue to provide insight into their values, decision-making, concerns, and hopes. And, thank you to the authors of the narratives in continuing editions of this workbook. Finally, thank you to those who found previous editions of this workbook useful in their planning and took the time to make improvements to this updated edition.

The original version of Planning the Future of Your Farm was created and developed by Robert Andrew Branan, an attorney in Hillsborough, North Carolina who concentrates his law practice in many things farming. The Washington State edition of this workbook, the first edition prepared for a western state, was pre- pared with help from Josh Giuntoli, Project Coordinator at the Washington State Conservation Commission's Office of Farmland Preservation, and from Washington State attorneys Duncan Greene of Van Ness Feldman and Dennis Brislawn of the Private Client Group, Ron Shultz, Policy Director at the Washington State Conservation Commission, and Laura Johnson, Communications Coordinator at the Washington State Conservation Commission. Supporting worksheets were inspired by numerous sources and have evolved through preceding editions of the workbook.

Funding for this edition was provided by The Specialty Crop Block Grant Program. The Specialty Crops Competitiveness Act of 2004 authorized the United States Department of Agriculture to make grants available to provide assistance for specialty crops, while the 2008 Farm Bill amended the act and authorized the USDA to provide grants to enhance the competitiveness of specialty crops. This workbook is the result of one of those grants and is meant to address estate planning for specialty crop growers in the state of Washington. It includes chapters on managing risk in the farm transfer process, improving family communication, evaluation farm resources, tools for farm transfer, and meeting with your professional advisors.

Farm estate planning is a tool for the preservation of farms in our state. Farm planning can provide for the continuation of farm operations in Washington, which contributes to the health of our state's specialty crops, overall agricultural economies, and local communities.

The information contained within this book is intended for use solely as an educational tool and research aid. It is not intended to be legal advice, nor is it intended to be a substitute for legal services from a competent professional. To obtain legal advice, please contact and consult with a licensed, practicing attorney. Further, the information provided in this publication is educational in nature and, as such, contains hypothetical's and other information for purely educational value that is fact-sensitive and results in different outcomes based on varying circumstances. Readers of this publication are encouraged to contact the authors for additional questions that may arise based on the educational content of this publication.

This book will also be available online at the Washington State Office of Farmland Preservation [http://ofp.scc.wa.gov/] and Cascade Harvest Coalition [http://www.cascadeharvest.org/].

Front and Back Cover photos appear courtesy of Washington State University.

Planning the Future of Your Farm (Washington Edition) was created, written and published by Andrew Branan, Lawyer, The Branan Law Firm PLLC (www.brananfarmlaw.com)

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About The Washington Edition

Planning the Future of Your Farm is a workbook for those families who *want* to keep their farmland in production and/or "in the family" as it passes to the next generation. The workbook is for those willing to commit the effort required to manage such a ongoing project. The workbook you are holding has been updated and adapted for Washington from previous editions published in North Carolina, Georgia, Virginia, and Pennsylvania. Feedback from families using earlier versions has been incorporated into this edition.

Planning and managing the orderly distribution of family land is a long term project that addresses challenges as they emerge. It is more than simply getting a set of legal documents signed: it is an ongoing series of transactions executed inside a flexible framework. Planning a future for your farm and land requires articulation of your goals, understanding the value and utility of your wealth, and a fair comprehension of the goals and life challenges of your family members. This workbook focuses heavily on getting prepared to effectively manage the legal process for transferring real property and working farm assets across generations.

One question stands out everywhere, persistent and perplexing: Who will farm the land?

The planning process also requires the help of professional advisers. This workbook was developed to help families communicate and harness information by gathering it into an orderly and productive process, maximizing the value of professional planning help. Under good guidance this process should produce the legal documents necessary to manage the risks of farm transfer.

Like the farm transfer process itself, the development of the *Planning the Future of Your Farm* workbook series has been a continuing and expanding project to help address issues that are at once local, regional and national in scope. It began as an effort to harness useful materials related to farm succession that were spread in many different sources across the country. The first collections of materials (copied into 1" binders) were initially used in the farm succession education campaigns begun in 2004 in Virginia and North Carolina. The collection evolved into a bound workbook, which has been updated and adapted to an ever-growing region, keeping pace with changes in (mainly) federal tax law. The copy you are holding was adapted specifically to Washington with review from Washington-licensed lawyers.

The workbook has been continually defined by the questions and concerns that farm succession education campaign participants bring to meetings, in groups and at the kitchen table. Many are concerned about specific tax and legal issues of estate planning, others about conservation income options, still others about the roles and trustworthiness of professional advisers. As the number of farmers has declined in the generation born since World War II, many families came to workshops wondering what to do with a farm when there was no one else in their family dedicated to the enterprise.

This edition, adapted and published for the Washington Conservation Commission's Office of Farmland Preservation, helps address the one question that stands out everywhere, persistent and perplexing: *Who will farm the land*?

Planning the Future of Your Farm certainly helps those who already know the answer, and can be used as a guide through many challenges. The workbook also addresses this question for landowners willing to search for that answer. This workbook can support the decisions of landowners who value that their land stay in farming, and are thus willing to offer land lease or purchase terms to help new farmers get established.

For newer farmers, the opportunity afforded by workshops that bring an ownership generation in the room - while challenging them to think about the future of their land - cannot be underestimated. Newer farmers - those at the beginning of their career that are seeking a farming opportunities - can meet older landowners in an atmosphere where all parties are learning about planning challenges and how to overcome them. Who knows what could develop?

Andrew Branan, Editor
April 2014

How to Use This Workbook

The Planning the Future of Your Farm workbook is laid out in four sections, each with narratives supported by worksheets. The workbook is primarily for use by specialty crop farm families (i.e., families that actively farm or that simply own a specialty crop farm). Families can use it themselves or under the guidance of a professional adviser. The workbook is also designed to support curricula in farm transfer workshops for farmers and landowners. Each section corresponds to a suggested planning process.

SECTION ONE, **Developing Your Vision for the Future**, discusses what we call the 'soft issues' — those that are the most difficult to discuss in daily discourse or over long distances and can often be ignored absent a forum for their discussion. The articles in this section offer perspective on the process you are undertaking, stressing the nature of risk management and what you are accomplishing by protecting your wealth and the relationships within your family. Section One includes several worksheets to note, including:

1) **"Rating Family Values"** (p 17): Questions to get you thinking — or affirm what you are already thinking — about the planning process and distribution of farm assets to the next generation. It also provides a format for your family to express their values in a forum where everyone's feelings are respected.

2) **"Rating Your Comfort Level"** (p 18): An exercise to gauge where you are currently in your thinking on the transfer process. This is a measure of your risk tolerance, which will govern decisions related to transferring farm assets. This worksheet will be most applicable for those looking to pass and take over a farm operation and less relevant for off-farm heirs. But, it can be reviewed by off-farm heirs with an interest in the issues and risks faced by those in a farm business transfer.

3) **"Setting Goals and Objectives"** (p 25): This self-explanatory worksheet is for the entire family. The following worksheet, "Reconciling Priorities," is designed to help put different family members' goals in one place and identify where some goals may conflict as they relate to a transfer of the farm.

4) **"Sketching Your Lifestyle Plan"** (p 20): Write down your thoughts on how you would like to allocate your time later in life with an eye toward what your disposable income needs will be and whether farm assets will be needed for this purpose.

5) **"Quick Risk Assessment: the 5 D's"** (p 14): Jot down perceived risks to your vision of keeping the farm in the family, keeping land in production and in the community, transferring a business, etc. based on the input from family members on previous worksheets and the steps you believe you've taken — or think you could take — to alleviate these risks.

SECTION TWO, **Evaluating Your Farm Resources** includes a primer on property ownership, one of the first steps in the evaluation of your resources. How you own property ultimately determines what decision-making ability you have over the resource. Worksheets in this section offer space and suggestions for you to rate the features of your farm, community, and family resources and skills. Use the worksheets to identify features that need improvement to support your business model for farm resources. The extensive "Farm Asset Net Worth Statement" worksheet (p 39) is for current operations to determine the financial health for expansion and transfer and realistic orientation on current asset liabilities.

SECTION THREE, **Farm Transfer Tools**, discusses different types of business entities for agriculture, forestry, and horticulture ventures, and some of the tools and agreements you will encounter in the estate planning process. The worksheets are designed to help you organize the information you will need to construct these agreements.

SECTION FOUR, **Preparing to Meet with Professional Advisers**, contains worksheets similar to those a professional adviser (financial planner or attorney) will have you complete as part of their service to you. These will let you start the process earlier and will save you time and money. And, it will show your advisers that you are on your toes about this planning process.

The workbook closes with the definitions of common legal terms relating to land ownership, business entities and estate planning.

Section One:

Developing Your Vision for the Future

A Proposed Definition

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

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

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

"The Plan is Nothing. Planning is Everything."

Dwight D. Eisenhower

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

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

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

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

Starting with What You Want

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

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

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

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

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

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

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

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

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

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

Photo courtesy Washington State University

Managing Risk In Farm Transfer: The D's

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

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

Planning to manage the D's

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

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

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

Death

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Disagreements and Disengagement

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

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

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

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

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

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

Worksheet 1.1

Quick Risk Assessment: the D's

Each family member should use this worksheet as a preliminary assessment of the 5 D's and how they could affect your *current plan* - or simple goals - for your future and the future of your farm. Start by keeping in mind the business, family, and personal goals of your family members. List the present plan in the column titled "Current Risk Management Plan"; for example, a document you currently have in place like a will. Next list the risks not addressed in the next column. Rank the possibility of this risk occurring in the next column. Then consider the impact on meeting the identified goals if this event were to occur. After completing these columns the 5 D's rank the risks in priority from 1 to 5 or as high, medium, or low. The last step is to identify steps to take to manage these risks. These steps become the building blocks of your farm transfer plan. The plan should be reviewed and updated as changes occur in the business or the people involved, and as goals change.

Risk	Current Risk Management Plan	Risks not currently addressed	Probability of risk at present	Impact of event on current plans	Steps needed to manage risk
Death					
Disability and Disease					
Disaster and Debt					
Divorce					
Disagreement and Disengagement					

Improving Farm Family Communication

Users of this workbook - particularly Mom and Dad - may want to seek input from family members in order to develop a shared vision for the future of the farm. At the end of the day, Mom and Dad must decide what to do with the farm assets. However, many times some decisions cannot be reached without input from other family members. Indeed, as emphasized throughout this workbook, keeping a farm in the family requires agreement between generations, which cannot be achieved from one side of the generational equation.

Keeping a farm in the family requires agreement between generations, which cannot be achieved from one side of the generational equation.

Often where there is open discussion about the future of a family business -- and more specifically, the value of its land assets -- there will be differing opinions on how it should be used or otherwise treated. Rather than hope that everyone will be in agreement with what is proposed for the farm, you should accept that differing opinions will be part of this process. If you do, perhaps when decisions are ultimately reached and documents executed, everyone will know where those decisions came from and be more likely to support them.

If one can suppose that conflict leads to stronger agreement, communication is the fire that forges the end product. It may be helpful to think of communication as a loop, from sender to receiver and back again, encompassing six elements: sender, message, receiver, channels, feedback, and effect. The sender sends a message through a channel -- verbal, written, or non-verbal -- to a receiver, who will then respond through the same or another channel (or not respond, itself a response). When received, the sender can determine if the message was understood, or otherwise process the effect of the response. The loop requires diligence among participants to avoid breakdowns and misperceived communication throughout, which of course entrenches disagreement (the biggest of the D's when it comes to farm transfer).

A few common sense ground rules can be agreed to by all parties so that the process does not break down. Here are a few items to keep in mind:

1. **Every message can be misinterpreted.** This is the situation where a sender has sent the message, but the receiver is unclear as to its meaning. If the receiver does not respond, the sender may either get the message that their position is understood, or that they are being ignored. At the get-go, all parties should agree that non-response to their position is not an affirmation that their position is correct, or otherwise agreed to. Even a non-response can be interpreted wrongly, or a non-verbal response (if in person) such as a furrowed brow will create its own message. All parties should adopt a stance of prompt feedback, even if it is to simply acknowledge receipt of the message and let the sending party know if they need time to consider or gather more information.

2. **Please never utter the word "non-negotiable."** Sometimes, this is the first thing someone will say to draw their "line in the sand." It is a bullying technique that by its very nature destroys trust, and carries with it no information useful in developing mutual agreement. It sends the message that what anyone else has to say is valueless. Try to avoid using it at any point in a family discussion.

3. **Be honest about your motives.** Nothing can be more frustrating than flowery language or idealistic imagery in a discussion about land and money. One reason to encourage family members to explore their own personal values about conservation and farming is to help folks be honest with *themselves* about what they want to see happen to the farm. Until this happens, explaining why you want something will be very difficult if that explanation is needed to educate other family members about your own position.

4. **Pay attention to listening skills.** Good listening skills can be improved by 1) simply making the decision that you will listen, 2) refraining from interrupting or immediately reacting (verbally or with body-language) to what is said by the speaker, 3) providing some form of positive feedback that you understand what the speaker is saying, maybe even to the point that you understand why they have their

position. All of this requires self-discipline.

5. **Communicate in an environment without distractions.** People are busy, and it is difficult to set aside time away from everyday tasks and deadlines. However, distractions that interrupt the back and forth flow of communication leave important questions unresolved, and often these are hard to revisit if progress is indeed being made between the parties. Family meetings, meetings between business partners, and meetings between a landlord and tenant should all be held in an environment where foreseeable distraction is minimized (ie. young children, a busy farm shop, etc.)

6. **Try to speak the same language.** This can be particularly challenging in farm planning situations, where not all parties to the discussion are farmers. Farm issues and terminology can get very technical, particularly when discussing yield conditions, input requirements and costs, equipment depreciations, commodity markets, etc. This applied equally to non-farm participants that have their own professional expertise, perhaps in law or investing. As best as possible all parties should realize that each does not necessarily possess the same expertise, and be prepared to explain the rationale that forms the basis for their opinions or positions.

With those tips in mind, it has been suggested that there are three dimensions where disagreement can develop. First there is the **substantive**. This is the nuts and bolts, the detailed outcomes of decisions such as ownership, management, organizational structure, timing, taxes, division of income and wealth (often the details relating to right to income from, authority to manage, and division of equity in that wealth). The second dimension is **relational**: people's feelings, emotions and differing perceptions of themselves and family members that often cloud rational decision-making on the substantive issues. The third dimension can be summarized as **process**. Often disagreement can flow from perceptions of fairness in the decision-making process, including the adequacy of gathering and sharing of information and alternate viewpoints, and when certain relationships create a perception of inequity.

Often the dynamics of disagreement are predictable, and disagreement in any of the three dimensions described above can lead to antagonism. Lifelong relationships can infuse disagreement with suspicions and questions about the other person's motives. As suspicions are shared among the like-minded, and not those we are suspicious of, silence broadens the gap and the ultimate cost of resolution. As noted earlier in this workbook, in the complex discussion about the future ownership of land, it is ultimately counterproductive to outsmart your siblings by being less than forthcoming about your motives.

Often the relational may be damaged by decades of sibling rivalry. The substantive may equally prove elusive due to differing fortunes throughout the lives of children reaching adulthood and having families of their own. In this instance, perhaps it is the *process* through which family can find common ground. Indeed, that is the focus of this section of the workbook, since we cannot alter the history that underscores the other two elements (ie. relationships and wealth needs).

In closing, a workshop held years ago in Albemarle County, Virginia offered an interesting visual demonstration about communication. A presenter was presenting on this subject before an audience of farm families. On a whiteboard, he drew a table with stick figure on either side, noting that this is how we often view discussions over an issue, with two sides of negotiation. He then redrew the picture with the stick figures on the same side, looking at the problem on the table. The presenter, Mr. Larry Hoover, a law professor at Virginia's Washington & Lee University, told the audience:

> *Negotiation is the predominant conflict resolution process, but unfortunately the adversarial, win/lose model imported from the legal system is too often adopted. What's needed is an interest-based, collaborative process, the important component of which is mutual empathetic listening to understand the interests, needs and priorities of others, while gaining clarity about our own. We must also search for creative additional value to bring to the table, which may depend on differing needs, valuations or time preferences, and use this information to feed a brainstorming of possible solutions and evaluating of options.*

His point: the more effort invested in addressing the issue of farm transfer as a shared family interest, the less energy (and money) will be expended on negotiating the outcome from identified positions.

Worksheet 1.2

Planning the Family meeting

Meeting with family to discuss important issues relating to the farm may be helpful in establishing and meeting your goals. This worksheet is to help you get everyone to the kitchen table, with an agenda to guide the discussion in a business-like fashion.

Target meeting date: ____________________ Place: ____

Time start: ___________________________

Persons needed to attend:	Date contacted:	Best dates to attend:

Proposed agenda:

____

____

____

____

____

____

____

Suggested preparation tasks	Person(s) responsible	Target completion date
1.		
2.		
3.		
4.		
5.		
6.		
7.		

Worksheet 1.3

Rating Family Values

To help start your planning, read and rate the questions below. Rate the importance of each item, with 1 = not important, 2 = somewhat important, and 3 = very important. You can use these ratings to support your family discussion. Have each family member complete the worksheet to help get a clearer picture of what is most important to each in the farm transfer process. Conflicting values can then be discussed.

I want the farm to remain in our family's possession. *Why is this important/not important to you?*	1	2	3
I want the farm to continue to be farmed after I/we retire. *By who?*	1	2	3
I would like to remain physically involved in the farm after I/we retire. *Why is this important/not important to you?*	1	2	3
I want our children to have the opportunity to continue management of the family farm. *In what capacity?*	1	2	3
I would like the division of farm property to be equal in dollar value among our children.	1	2	3
I want the division of property among our children to be fair (not necessarily equal).	1	2	3
I want to give financial help to our children who choose a farm career.	1	2	3
I want to have the financial resources to do new things after farming. *What do you want to do? (see Sketch Your Lifestyle Plan)*	1	2	3
It is important that our children agree with our plans for the farm's future. *Why is this important/not important?*	1	2	3
I would like to maintain some measure of financial control over the farm while I am alive. *Reason:*	1	2	3
I would like to be involved in the decision-making of the farm throughout my life. *Reason:*	1	2	3
I want to receive what the farm is worth when it is transferred. *What is your farm worth to you? (E.g. full market value?)*	1	2	3
I want our children to play a part in the decision-making for the farm's future. *Why is this important/not important?*	1	2	3
I would like everyone in the family to be satisfied with the plan for the future of the farm.	1	2	3
It is important to me that our children's requests regarding the farm transfer be honored.	1	2	3

Worksheet 1.4

Rating Your Comfort Level

It's a given that risk tolerance differs between generations. The senior members of the farm family are quite justified in their concern about protecting what they have. Confidence in their own ability to manage resources to meet their own needs often eclipses their ability to transfer management to the next generation. Likewise, the younger members can see the necessity that their ideas and energy be put to work earlier to grow and secure their income interests. Agreement is not easy, but exposing risk tolerance levels helps each generation understand the other. The table below contains a list of possible actions for your farm during/after the farm transition process starts. Please rate your personal level of comfort for each of these actions on a scale of 0-10 (Zero indicates you are very uncomfortable with taking that action; 10 indicates you are extremely comfortable with taking that action). Each member of the family that is interested in managing the farm should fill out this form and compare. Add your numerical responses, and divide by eleven (11); the resulting figure is your "risk basis" of how far each of you have to go in reaching a consensus. Use each statement above as a platform to discuss your ideas on changes you would make in management of the farm resources.

Expanding the size of the current operation	1	2	3	4	5	6	7	8	9	10
Reducing the size of the current operation	1	2	3	4	5	6	7	8	9	10
Taking on added debt to expand	1	2	3	4	5	6	7	8	9	10
Adding new enterprises	1	2	3	4	5	6	7	8	9	10
Eliminating one or more enterprises	1	2	3	4	5	6	7	8	9	10
Making dramatic changes to the operation	1	2	3	4	5	6	7	8	9	10
Taking more time away from the operation	1	2	3	4	5	6	7	8	9	10
Increasing the amount of management you provide to the operation	1	2	3	4	5	6	7	8	9	10
Increasing your managerial responsibilities	1	2	3	4	5	6	7	8	9	10
Relinquishing managerial responsibilities	1	2	3	4	5	6	7	8	9	10

Worksheet 1.5

Sketching Your Lifestyle Plan

As you consider the long term future, it might be helpful to sketch out what you would like to do as your farm responsibilities wind down in later years. In farming, retirement can be a vague concept, as it often simply means transitioning to less labor, management, and risk-intensive activity. Nevertheless, this exercise may serve to help in situations where parents are looking to articulate how they would like to spend their time away from farm work and management to make room for use of the land by another family member or tenant. Though space is limited, jot down a few ideas in the grid provided, and use other paper to further explore your ideas.

Activities	What will you do and where will you do it?	How much time per week? (or which months)	Related expenses (dues, clothing, travel, material)	How will your health affect your planned activities?
Farm work				
Involvement in organizations (church, Farm Bureau, etc.)				
Second career				
Special interests and hobbies				
Travel				
Visiting with friends and family				

(Inspired by *Business Planning for Farmers: Planning the Late-career, Retirement-mode Years*, Midwest Plan Service, 2003)

Worksheet 1.6

Estimating Income and Expenses

Use this worksheet to estimate your annual living expenses. This is useful to get a real grasp of your retirement income and expenses, or if not nearing retirement, your annual living and income needs.

Part I: Income	**Current**	**Expected**
Wages (Annual)		
Social Security		
Pension/IRA/401K		
Social Security		
Net Farm Income		
Other Business Income		
Rent/Lease Income		
Conservation Program Income		
Forestry Income		
Taxable Interest		
Tax-Exempt Interest		
Stock Dividends		
Annuity Payments		
Other (e.g. alimony)		
Total Gross Income		
Estimated Taxes		
Federal		
State		
Medicare/Social Security		
Total Taxes		
TOTAL NET INCOME		
Part II: Expenses	**Current**	**Expected**
A. Housing		
Gas/Oil/LP		
Electric		
Real Estate Taxes		
Mortgage Payments (P+I)		
Home Equity Line		
Home-Owners Insurance		

Expenses Cont'd	**Current**	**Expected**
Rent		
Homeowner dues		
Water/Sewer/Garbage		
Telephone		
Maintenance and Repairs		
Lawn Care/Cleaning		
Miscellaneous Household		
B. Food/Clothing/ Transportation		
Food/Groceries/Supplies		
Clothing		
Laundry/Dry-cleaning		
Auto Loan/Lease		
Auto Insurance		
Gasoline		
Auto Maintenance/Taxes		
Public Transportation		
C. Discretionary		
Charitable Contributions		
Movies/Concerts/Dining		
Recreation/Vacation		
Gifts (birthdays/holidays)		
Children sports/lessons		
Pet Veterinary		
Cable Television/Internet		
Sub-Total Expenses (this page)		

Expenses Cont'd	**Current**	**Expected**
Sub-Total From Previous Page		
D. Insurance/Medical		
Health Insurance Premiums		
Co-pays, Deductibles		
Disability Insurance Premiums		
Life Insurance Premiums		
Long-term Care Insurance Premiums		
E. Other Expenses (List Below)		
Total Expenses		
TOTAL NET INCOME		
(Subtract)		
TOTAL EXPENSES		
(equals)		
TOTAL DISCRETIONARY INCOME		

NOTES:

Developing Goals and meeting Objectives

A key challenge faced by farmers and landowners is the clear articulation of their goals and objectives to their professional advisers. Busy practitioners are challenged to spend enough time with clients to help them -- and their families -- explore their goals and objectives and identify hidden and potentially conflicting goals. The more work that can be done to articulate goals and objectives before meeting with advisers, the better they will be able to help you. Indeed, the many decisions of farm transfer are built on a clear understanding of a shared vision. This can only be achieved by the exercise of writing down goals and objectives. Generally, you should think of goals as long term (5 to 10 years) and objectives as those shorter-term achievements that take you to your goals. Tasks are your specific "things to do," and though you may not know exactly the tool you need to accomplish the objective, your professional advisers will help you with those tasks The following worksheets should provide a platform to get you and your family started.

Your goals and objectives for your estate are yours alone, and the goals and objectives of your family members may be different from yours. You, the owner of the farm, will ultimately create the will and make the estate decisions. Nevertheless, discussion of your goals and the desires of family members and business associates can reduce the likelihood of strife during the transfer.

After you have a feel for your own goals and those of your family, sit down and list your individual objectives in achieving these goals. Rank your objectives in order of importance. Consider the suggested bullet lists below as a guide. Once your objectives are clearer, your professional adviser will have a much better time of ensuring your estate plan works and is adaptable to meet your goals.

The list below reflects common goals followed by objectives to reach those goals associated with farm transfer and estate planning. You and your family's goals and objectives are as varied as the individuals who have estates to plan. Not mentioned are the less laudable objectives that can include using one's estate plan to manipulate friends, relatives and business associates, or to take revenge. Be careful while planning your estate to avoid unforeseen consequences that may result in litigation over your estate after your death. If you fear your estate will be embroiled in controversy, be sure to alert your financial counselor or legal adviser. This is not a complete list, and is meant only as a guide to get you going.

A sampling of suggested goals, objectives and associated tasks:

GOAL: Provide security for your surviving spouse.

OBJECTIVE: Relieve your surviving spouse of management responsibilities.

TASK: Provide management flexibility for your surviving spouse in a trust.

TASK: Nominate a guardian or draw up a durable power of attorney and nominate an agent in the event of your own disability.

OBJECTIVE: Retire at a specified age (for example, 50, 60, or 70).

OBJECTIVE: Provide security for both spouses after retirement.

TASK: Make advance decisions about end-of-life issues including whether to terminate life support, whether to use alternatives such as hospice care, and whether to use certain medical technologies.

GOAL: Assure continuity of a farm, ranch, or other businesses.

OBJECTIVE: Protect business associates and the business from adverse consequences of your death.

TASK: Review the current operation and ownership of the farm, ranch or other business, and restructure as needed to promote sound business management.

TASK: Purchase investments and insurance that minimize the financial consequences of your incapacity or disability.

TASK: Transfer property during your lifetime by means of business entity interest gift.

TASK: Provide for the payment of the estate's taxes, debts, and expenses.

TASK: Transfer specific property to specific heirs or others.

TASK: Nominate a health care agent to make health care decisions in the event of your incapacity.

GOAL: Transfer as much of your wealth as possible to your chosen heirs.

OBJECTIVE: Minimize other taxes, including income, property, and gift taxes that may adversely affect you, your business or your heirs.

OBJECTIVE: Provide for coordination between federal and state taxes to minimize the overall tax burden.

TASK: Reduce income taxes through re-organization of income producing property during your lifetime.

TASK: Transfer assets to a trust to minimize expenses associated with settling an estate.

OBJECTIVE: Provide financial and physical security for an incapacitated heir.

TASK: Have a lawyer create a special needs trust to allow incapacitated heir to receive necessary support payments.

TASK: Nominate guardians or designate trustees for minor children and/or an incapacitated heir.

TASK: Nominate executor(s) of your estate.

GOAL: Provide equitable (although not necessarily equal) treatment of children.

OBJECTIVE: Make gifts to heirs and others during your lifetime.

TASK: Transfer non-titled personal property of significant emotional value but little monetary value in a cost-effective manner that satisfies heirs.

OBJECTIVE: Plan division of real estate.

TASK: Inventory real estate holdings, determine values from property tax assessments, consider needs of farming heir in farmland, consider distributing non-farm land to other heirs.

TASK: Update will and/or trust to reflect specific distribution plans.

Worksheet 1.7

Setting Goals and Objectives

Use this worksheet to write down your long-term goals, what you want to do over the next ten years. Then take a shot at drafting shorter term objectives you think are necessary to achieve these goals. Try as best you are able to separate your personal goals and your goals for the management of the farm (ie. your involvement in the income the farm produces, passively or as a family farm business). Make copies of this sheet and have each family member fill it out for discussion at your family meeting.

Long Run Goals (5 to 10 years)	
A. Personal	
1	
2	
3	
4	
5	
B. Farm, other business or career	
1	
2	
3	
4	
5	
Shorter Term Objectives (12 months to 2 years)	
A. Personal	
1	
2	
3	
4	
5	
B. Farm, other business or career	
1	
2	
3	
4	
5	

Worksheet 1.8

Reconciling Priorities

Use this worksheet to summarize the discussions and agreements reached in a family conference. This is done after you have reviewed and discussed the objectives and goals from the “Setting Goals and Objectives” worksheet filled out by each family member. Focus on the most important goals and objectives for each family member, and identify the common ground and where potential conflicts exist.

Have each family member rank their top 2 longer-run goals	
Name	Brief description of goals
	1.
	2.
	1.
	2.
	1.
	2.
	1.
	2.
	1.
	2.
List the SHARED goals and note whom they are shared by	
List the potential CONFLICTING goals identified above	

Worksheet 1.9

Turning Goals and Objectives into Action

Now that you have identified longer term business and personal goals in the previous worksheets, and hopefully met to reconcile priorities among each family member's goals, use this worksheet to further identify the actions steps for each goal and objective, followed by a person responsible and when the tasks should be completed. Task deadlines should be set in advance of a next scheduled meeting.

Goal	Objective	Action Steps	Person(s) Responsible	Deadline

This layout was inspired by Wise, D.K. and Sneed's, C.T. Retirement Planning: Realities and Resources. Chapter in Planning Today for Tomorrow's Farms. The University of Tennessee.

Notes

Section Two:

Evaluating Your Farm Resources

Photo courtesy Washington State University

Evaluating Your Farm and Community Resources

As noted earlier, this workbook is built on the premise that your family wants to retain ownership of your farm in the next generation, or otherwise wishes to see it continue in agriculture or forest use. In developing plans for the future of your farm, it is important to determine what type of production enterprise - if any - the farm, family, and the community surrounding it will support. Alternatively, if you will not actively manage an enterprise on your land, your decisions will nonetheless depend on the opportunities for its use by someone else.

In many cases, the next generation -- someone in the family perhaps -- has plans for what they want to do with the land, whether they will own it outright or with other family members. They may already be farming the land, with their parents or by themselves, and will likely continue to follow the current business model which must expand to support more than one family. In other cases, the next generation will have new ideas, be looking for new markets, or may even be coming back to the farm from another career to make use of the land for income. In either case, an important part of the succession discussion will be an assessment of whether your land and community resources will support present or alternative land uses in the future.

An important part of the succession discussion will be an assessment of whether land and community resources will support present or alternative land uses in the future.

The Quantity and Quality of Land and Water
Land can be looked at from two perspectives, the quality and quantity. First, if you are planning an enterprise, factors such as the soil quality, drainage characteristics, and the quantity and quality of water available, all impact what type of operation you will be able to develop. Different soils are good for different types of production, and different crops may be suitable depending on the amount of water available for irrigation. You should take the time to carefully evaluate both the amount of water that is physically available for irrigation as well as the amount of water that is legally available under the water rights associated with the land. Second, the amount of open land available - what you own or what is available for rent - will influence your plans for scale of operation.[1]

Working Infrastructure and Capital Position
What is the state of your current working assets, such as machinery, buildings, and fencing? In most farm production there is a need for storage for equipment, livestock, feed, fertilizer, fuel, and crops. Likewise, for livestock operations, are the current fencing arrangements adequate? Also, particularly for existing enterprises, what is the capital position of the business in terms of liquidity and solvency? Important also is the availability of credit, which is dependent on the borrower's -- whether the business or individual -- present financial position, the profitability of business alternatives, and credit rating. Financing, of course, depends on one's ability and willingness to manage debt.

Personal Management Capacity
Management capacity is not a given, and will probably be one of the most sensitive discussions the family will undergo. Mom and Dad are making decisions based on love, but even those should take into account whether potential heirs or business successors have the personal wherewithal to manage land and/or a business responsibly (particularly if sharing ownership with siblings). Indeed, many estate plans create a trusteeship over property in one of the heirs, a position of great responsibility.

Where families are looking to gradually transfer a business between generations, an assessment should be made of both generations' abilities, to look for complementary skills and productively identify areas of improvement. When a family will keep but not actively farm the land, someone will still need to manage tenancies and pay taxes. You should assess

1 Additional information regarding water rights can be found at the following web sites:

- http://www.ecy.wa.gov/programs/wr/rights/Images/pdf/landownerguide_2009-2ndEd.pdf
- http://www.ecy.wa.gov/programs/wr/rights/find_existingwr.html

the management capacity of each family member for this purpose.

The Quantity and Quality of Labor and Tenants If someone in your family plans to operate an enterprise on the land, who will supply the labor? Any enterprise will necessarily depend on family labor, or hired outside labor. Questions to consider include how much time family members will be able to devote to the enterprise, particularly if working an off-farm job, and whether there is an affordable labor pool in the area, one that the enterprise model can support. If you are looking at working with another producer -- as a tenant or a potential partner -- how will you meet like-minded individuals in your area?

In many farming areas, the competition for land is competitive and fairly straightforward, built on relationships and who will pay the highest rent supported by commodity prices. In other areas, finding a suitable tenant can be more of a challenge, depending on their business model and experience, and the factors they require in building an enterprise on your land. At some point, you will need to develop criteria for who you will want farming your land, based on your financial needs and personal values.

Local and Community Support for Farming
It has been said that no one has ever farmed alone. Commercial food production has always relied on community support. Many of the qualities that make farming attractive -- rural quiet, professional independence -- are nonetheless built on numerous variables that require community support. If someone in your family has a goal to expand production into new markets, it must follow an assessment of the infrastructure to support that business. Examples include proximity of processing, slaughter facilities, and direct market outlets (farmers markets, restaurants, individual consumers). Additionally, there may be developing distribution enterprises in the area in which the farm might participate.

As noted above, if your family wishes to keep land under family ownership but not actively farm it, you will need someone else to farm it. Does your land lie in an area where there is an active tenant market? Is there enough local support to help a tenant grow a business on your land?

The factors identified in the proceeding worksheets are designed to get your family thinking about what is available and what is needed. Ultimately, this assessment will support plans for transfer of the farm.

Photo courtesy of Washington State University

How Do You Own Your Property?

One crucial part of assessing your resources for farm transfer planning is understanding who has ownership rights in the property -- both real and personal -- that you have at your disposal for personal and farm use. Ownership interests impact how property is passed to heirs, what their rights in it will be, and what decision-making authority you and other potential owners have in the property.

Property is divided into two classes: real property and personal property. Real property consists of land and certain kinds of interests in land. Real property includes structures erected on the land, such as a house, fences or barns. Personal property is everything that is not real property, such as cash, farm equipment, livestock, nurserystock, harvested timber, and household items like cars, jewelry, bank accounts, stocks and bonds.

Evidence of Ownership: Real Property
Ownership or title to real property is normally shown on the deed to that property. However, there are times where you may own an interest in real property where no deed exists, such as when you inherit land through an estate and no deed is drawn up. For real property, the document of title (warranty or other deed) or interest (e.g. easement deed) must be registered according to the state recording act, which determines in what form and where interests in land must be recorded. The state recording act also dictates priorities in land ownership. Deeds to real property must always be recorded in the Recorder's Office for the county where the land is located.

Title to the same parcel of land can be held by one or several people, and in different percentages of ownership depending on how and when the land was transferred. If your name is the only name on the document of title, you are the sole owner of the property. If your name and someone else's name appear on the document of title, your ownership rights are likely limited by the rights of the other owner.

The document of title may create *consecutive* interests in the same property, in other words, when one person's title ends, the other begins as a matter law. The most common example of this is a life estate deed, where one owner, often a surviving spouse, has the ownership of property so long as he or she lives, and when he or she dies the ownership is immediately transferred to another person or persons, usually the children of the life tenant. A document of title may create *concurrent* interests, where the rights of each owner occur at the same time. Both consecutive interests and concurrent interests can take various forms, giving different property rights to the owners.

Evidence of Ownership: Personal Property
Ownership of personal property may be shown by automobile titles, receipts, contracts, bills of sale, bank records, stock certificates, etc. Without these documents, ownership of personal property may be difficult to prove. In many cases, particularly for tangible items, possession of personal property may count as proof of ownership, or at least making ownership harder to disprove by another claiming that property.

Personal property can be either tangible or intangible. Tangible personal property is something physical, such as a tractor, a cow, a car, or a gold bar. Cash in dollar bills tucked away in a dresser drawer is tangible personal property, whereas money in a bank account is intangible personal property. Intangible property is something that requires a piece of paper to describe what it is and in what quantity it exists.

Sole ownership
Sole ownership is the simplest form of property ownership, where one person has all present and future power to use, control, sell or otherwise dispose of the property. If you are the sole owner, you may transfer the entire property under the terms of your will, or place your entire interest in a trust. If you do not have a will, your property will be transferred under the state intesticacy act (see *Basic Estate Planning Documents: Wills, Trusts and Gifting*, page 49).

Consecutive interests
If you are the sole owner of real property, you record a deed that creates consecutive interests in the property. A life estate deed that transfers your interest to another upon your death is the most common example of consecutive interests. If you create a life estate, you are called the life tenant. You have the right to possess and use the property for the life of a specified person.

Usually, a life estate is measured by the life of the life tenant, but it may be measured by the life of someone else. If so, the life tenant's interest ends upon the death of that person. Upon your death (or the death of a specified person), ownership passes to the person or persons who own the remainder. They are called remaindermen.

Usually, the life tenant has the following rights and duties, unless the document creating the life estate shows a contrary intent.

- A life tenant may sell his estate for life. The purchaser buys the right to use and possess the property for the lifetime of the life tenant or specified person.

- The life tenant has the right to plant, harvest and sell annual crops.

- Fee title to the land itself may not be sold unless the life tenant and all the remaindermen join in the sale (though a remainderman may sell his or her interest subject to the life estate). If the property is unproductive, the life tenant may seek permission from a court to sell the land. A court would grant such permission only in unusual cases, however, and the court would require the life tenant to reinvest the funds for the benefit of the life tenant and the remaindermen.
.
- The life tenant is responsible for taking care of the property and for making ordinary repairs, and must pay property taxes and local assessments. If the property is mortgaged when it comes to the life tenant, the life tenant is responsible for paying the annual interest on the debt, but not the principal.

- The life tenant may not give away the property under the terms of his or her will if his or her life was the measuring life.

An example of words in a will or deed that create a life estate can be "to my wife for so long as she lives, remainder to my nephew, James." The wife has the right to possess and use the property for her lifetime, and upon her death, the property passes to Jane as the sole owner.

Although it is easy to create a life estate, it cannot be undone absent the consent (by new deed) of the remaindermen. Furthermore, it is still part of your taxable estate for federal estate tax purposes.

Concurrent interests

If you have inherited property (ie. land) along with your siblings or others, you own a concurrent interest in the property along with the others. Concurrent ownership means your rights and the rights of other owners occur at the same time. Your rights in the property depend upon the form of joint ownership, and often how it was acquired. Concurrent joint ownership of property in Washington may take two forms: tenancy in common and joint tenancy with a right of survivorship. Of these two forms of ownership, only tenancy in common permits your interest in the property to pass under the terms of your will. As discussed below, however, ownership by tenancy in common can lead to complicated ownership patterns by multiple parties, making the land more difficult to market and sell.

Tenancy in common: A tenancy in common means that two or more people own an undivided fractional interest in the same piece of property. This is probably the most form of land ownership for inherited land in families with more than one child. For example, if three children inherited property from a parent "to share and share alike," they own the property equally as tenants in common, each owns an undivided one-third interest in the entire property, not a specific portion of it. Each co-owner has the right to use and possess the whole property, but each co-owner cannot exclude another co-owner.

None of the owners in co-tenancy may take any action with respect to the whole property without the written permission of the others. The agreement of all three is required to sell, lease, gift, or mortgage. Absent an agreement to the contrary, all co-tenants share equally in the income and rents produced by the property. For example, a deed signed by one owner does not transfer interest in the entire property, only their percentage ownership (and again, not to a specific part of the property). The new owner owns it along side the other tenants. Likewise, a lease to the entire property signed by one owner is likely unenforceable if the other owners do not also sign it.

Any co-tenant can ask a court to order a partition to the property. The court may be able to divide the property and give each co-owner a proportionate interest. On the otherhand, if the property is not easily partitioned

- usually the case with land of varying attributes such as crop land, water, woodlands and road frontage - the court can order a sale of the whole property. The proceeds of the sale are divided according to each co-tenant's interest.

Ownership shares in a tenancy in common can be unequal. This can happen when one of the co-owners dies and his or her heirs inherit their interest.

Example: *Brothers, Richard and James, inherited a farm from their mother who owned it as sole owner. Each owns a fifty percent undivided interest. Richard dies with a will that leaves his property to his five children to "share and share alike" whereupon his share is bequeathed equally to his five children. James still owns a fifty percent undivided interest, but now his nieces and nephews are his new co-owners, who each own a ten percent undivided interest in the property.*

Then James dies, leaving his undivided interest to his two children. Each of his children owns a twenty-five percent undivided interest, but there are now seven owners to the farm. To sell the entire farm, or even lease it to another farmer (absent an agreement otherwise) the seven cousins must agree to the sale. James' children have no greater authority simply because they own a larger interest. Further, any cousin may choose to sell his or her individual interest to a willing purchaser. If any one of the cousins dies, his or her interest will continue to pass to his or her heirs, and there may be more co-owners, now of differing generations.

The value of a co-owner's undivided interest is included in his or her gross estate for federal estate tax purposes and may be subject to federal and state estate taxes. The value of the interest is measured by the fair market value of the property multiplied by their percentage interest, although a discount may be allowed if there are more than a few owners.

Joint tenancy with right of survivorship: Two or more persons may own property as joint tenants with right of survivorship. This is common for bank accounts, certificates of deposit and stock certificates, particularly where an elderly parent wishes these interests to pass outside of probate, or they wish to have their money - in the case of a bank account - readily accessible by a chosen child to immediately handle matters following their death. Real property may also be owned jointly with a right of survivorship. To create a joint tenancy with right of survivorship, the document of title - say a deed - must expressly say the property is held with the survivorship right (the absence of such language simply creates a co-tenancy). However, this is no longer common outside of marriage (see below).

Upon the death of a joint tenant, in a joint tenancy with right of survivorship, the entire property automatically passes to the surviving joint tenant or tenants, and does not pass in the deceased owner's will or by intestacy.

Example: *Laura is a widow with two children, Caroline and Elizabeth. Laura is getting older and becoming concerned that she may forget to pay her bills. Laura goes to the bank with her youngest*

Photo courtesy of Washington State University

daughter, Caroline, and converts her account to a joint survivorship account, thus giving legal authority to Caroline to write checks and make deposits on her account.

The creator of a joint bank account should be careful to consider his or her other wishes as to the distribution of other property. Continuing the above example:

Laura had inherited two separate farms from her father, and in her will she has directed that one farm go to Caroline, the other to Elizabeth. Laura is made an attractive offer by the tenant on the farm designated for Elizabeth, and decides to sell it to him. She then deposits the sale proceeds in the joint bank account. When Laura dies, Caroline becomes sole owner of the sale proceeds, and still inherits the other farm through the will. Caroline likely has no legal obligation to share the money with Elizabeth. Such a situation could likely spawn litigation between Caroline and Elizabeth, which is probably not what Laura would want.

Conclusion

As you can see, the way you own your property affects your rights to use, manage, sell or direct its distribution after your death. Automatic survivorship takes precedence over what is written in your will, and a carefully designed estate plan can be defeated if you fail to consider how your property is owned when you make certain decisions about its disposition. There may be times in your planning process that it is advisable to change the form of ownership to achieve farm transfer planning goals. You lawyer will be able to determine how you own your property by looking up the deeds or otherwise knowing how and when you inherited it. It is not necessary to go into the lawyers office with deeds in hand. It is usually enough to inform him or her the counties where you *think* you own land, and he or she can do the rest. Hopefully, your lawyer will follow the wisdom of Dr. Neil Harl of Iowa State University, who cautions in his multi-tome treatment of agricultural law: You should never take your client’s word that the farm is in their name alone.

Worksheet 2.1

Evaluating Farm Resources

Earlier in this workbook, you worked on gathering information for what you want to see happen to the farm in the future. It is now important to look at what natural resources and farm infrastructure you have at your disposal. Use this worksheet to rate the overall condition of your farm resources, including the state of buildings, local agriculture support infrastructure, and the potential to expand and/or develop new markets.

Part I: Natural Resources

Resource	Poor	Adequate	Strong
Water availability (physical)			
Water rights (legal)			
Soils - quality			
Pasture land presently available			
Crop land presently available			
Timber quality			
Wildlife habitat			
Erosion control			
Other:			
Other:			
Other:			
Other:			
Other:			

Notes:

Part II: On-Farm Buildings and Infrastructure

Building 1:	Poor	Adequate	Strong
Current Condition			
Capacity			
Layout/Design			
Building 2:	Poor	Adequate	Strong
Current Condition			
Capacity			
Layout/Design			
Building 3:	Poor	Adequate	Strong
Current Condition			
Capacity			
Layout/Design			
Building 4:	Poor	Adequate	Strong
Current Condition			
Capacity			
Layout/Design			
Fencing			
Fuel Storage (tanks)			
Feed Storage:			
Crop Storage:			
Other:			

Notes:

Part III: Local and Community Infrastructure

Take some time and think about the community where your farm is located. Does it have the elements needed to support the type of use you envision for your land, or the type of enterprise you would like to operate on your land? Your assessment of local services and support is important to identifying gaps that with community attention could be improved.

Resource	Poor	Adequate	Strong
Availability of farm supplies			
Repair services			
Availability of financing			
Availability of business support (training, tax professionals, etc.)			
Competitive tenant market			
Availability of processing			
Competitive labor market			
Road system			
Local zoning policies			
County and Municipal government support of agriculture			
Community support of agriculture			
Local Farmers Market			
Urban pressure			
County economic development			
Availability of health services			
Timber Markets			

Notes:

Part IV: Farm Asset Net Worth Statement

Use this worksheet to sketch your farm's net worth. Later worksheets will help you estimate the value of your overall estate. Supply the information to the page below by completing the schedules [noted in parentheses] following. Note that not all schedules will apply to all situations and operations.

Farm Assets	Cost Basis	Market Value	Farm Liabilities	Market Value
Farm checking (M)			Accounts payable (N)	
Crops held for sale or feed (A)			Farm taxes due	
Investment in growing crops (B)			Current notes and credit lines (O)	
Commercial feed on hand (C)			Accrued interest - short (P)	
Prepaid Expenses (D)				
Market livestock (E)			Accrued interest - fixed (P)	
Supplies on hand (F)				
Accounts receivable (G)			Other current liabilities	
Other current assets				
Total Current Assets			Total Current Liabilities	
Unpaid cooperative distributions (H)			Notes and contracts, remainder	
Breeding livestock (I)				
Machinery and equipment (J)				
Buildings and improvements (K)				
Farmland (L)				
Timberland (L.1)				
Merchantable Timber (L.2)				
Pre-Merchantable Timber (L.3)				
Other fixed assets			Total Fixed Liabilities	
Total Fixed Assets				
a. Total Farm Assets			b. Total Farm Liabilities	
			Current Assets (market) Current Liabilities = _____ Ratio	
c. Farm Net Worth (a - b)				
			Current Assets (market) Current Liabilities = _____ Debt to Asset Ratio	

Part IV: Supporting Schedules

Schedule A: Crops Held for Sale or Feed				
Description	Unit	Price per Unit	Quantity	Value
			Total	

Schedule B: Investment in Growing Crops			
Description	Acres	$/acre	Value
		Total	

Schedule C: Commercial Feed on Hand				
Description	Unit	Price per Unit	Quantity	Value
			Total	

Schedule D. Prepaid Expenses				
Description	Unit	Price per Unit	Quantity	Value
			Total	

Part IV: Supporting Schedules (cont'd)

Schedule E: Market Livestock				
Description	Number	Average weight	Price per head	Value

Schedule F: Supplies on Hand				
Description	Unit	Price per Unit	Quantity	Value
			Total	

Schedule G. Accounts Receivable		**Schedule H. Unpaid Cooperative Distributions**	
Description	Value	Source	Value
Total		Total	

Schedule I. Breeding Livestock				
Description	Number	Average weight	Price per head	Value
			Total	

Part IV: Supporting Schedules (cont'd)

Schedule J: Machinery and Equipment						
Description	(a) Previous Cost Basis	(b) Cost of Purchases/ Trades	(c) Deprecia- tion	(d) Cost Basis of items sold	New Cost Basis (a+b-c-d)	Current market value
					Total	

Schedule K: Buildings and Improvements						
Description	(a) Previous Cost Basis	(b) Cost of Purchases/ Trades	(c) Deprecia- tion	(d) Cost Basis of items sold	New Cost Basis (a+b-c-d)	Current market value
					Total	

Schedule L: Farmland						
Description and number of acres	(a) Previous Cost Basis	(b) Cost of Purchases/ Trades	(c) Cost basis of land sold	(d) Cost Basis of items sold	New Cost Basis (a+b-c)	Current market value
					Total	

Part IV: Supporting Schedules (cont'd)

Schedule L.1: Timberland						
Description and number of acres	(a) Previous Cost Basis	(b) Cost of Purchases/ Trades	(c) Cost basis of land sold	(d) Cost Basis of items sold	New Cost Basis (a+b-c)	Current market value
					Total	

Schedule L.2: Marketable Timber						
Description and number of acres	(a) Previous Cost Basis	(b) Cost of Purchases/ Trades	(c) Cost basis of land sold	(d) Cost Basis of items sold	New Cost Basis (a+b-c)	Current market value
					Total	

Schedule L.3: Premarketable Timber						
Description and number of acres	(a) Previous Cost Basis	(b) Cost of Purchases/ Trades	(c) Cost basis of land sold	(d) Cost Basis of items sold	New Cost Basis (a+b-c)	Current market value
					Total	

Part IV: Supporting Schedules (cont'd)

Schedule M: Farm Cash on hand, Checking Account Balances, Savings, Securities, and Certificates			
Description	Bank/Institution	Number	Value
Farm Cash			
Checking Account			
Checking Account			
Savings Account			
Farm Securities			
Farm Certificates			
		Total	

Schedule N: Farm Accounts Payable	
Description	Value
Total	

Schedule O: Current Farm Notes and Lines of Credit			
Description/Purpose	Institution	Balance-owed	Accrued interest
		Total	

Schedule P: Fixed Farm Notes and Contracts						
Description	Interest rate	Date Due	Balance Owed	Due in 12 months	Remainder	Accrued interest
		Total				

Part V: Management (Human Resource) Assessment

This worksheet could certainly challenge your objectivity, particularly where family members are involved. Please duplicate for multiple relevant individuals, particularly if you are looking at business succession issues. This sheet is also useful for deciding who is best suited to handle important tasks like land management, entity management, etc. Duplicate, complete, and discuss steps that can be taken to improve challenging areas.

Skill/Trait	Comments
Farm production management	
Financial management	
Marketing management	
Personnel/Labor management	
Organization	
Scheduling	
Creativity	
Innovation	
Decision-making ability	
Ability to listen	
Logical thinking ability	
Work ethic	
Other:	
Other:	
Other:	
Other:	

Notes:

Notes

Section Three:

About Farm Transfer Tools

Photo courtesy of Washington State University

The Transactions of Farm Transfer

In Section One of this workbook, we emphasized the importance of exploring core values and developing a long term vision for the family's relationship to the farm. Also in that section, we discussed inherent risks to that vision: death, disability, divorce, disaster, and disagreement (the "D's"). If you consider these two concepts together, they demonstrate how the tools of farm transfer work.

Consider your life as a timeline, and identify two points: the "here and now" and the "there and then." If you have taken steps advised earlier in this workbook, both can somewhat be identified in your mind. Now, imagine one or more of the Five D's between those two points, and what happens to your vision when one of those things happens. The development and execution of estate planning and farm transfer transactions are what lawyers and other advisers prescribe to address the D's, the challenges to the future you envision. Because such events are foreseeable, legal agreements are meant to keep your wealth and your farm fairly intact as it is visited by a D risk event.

When it comes to agreements in farm transfer, it is helpful to consider that you are transferring three rights in an asset: Income, Management, and Control of Equity (ownership). The agreement you form with the person or persons to whom you are transferring the asset - say a farm - will govern all parties rights to these three things.

For example, when you transfer land, you transfer the right to earn income from it. If you sell it outright or make a gift of it, you completely relinquish your right to earn income from it. If you form a lease agreement with a farmer to use the property, you can retain income from the property in the form of rent, while the farmer receives the return on the sale of his or her crops. With a lease, you also allocate management while retaining control of the equity.

As outlined in this section, there are a number of legal instruments - wills, trusts, partnerships, limited liability companies, leases - that can transfer rights to assets. For some tools such as wills and trusts, one generation can decide what is going to be done with the assets without the consent (often without the input) of the heirs, and that generation simply lives with the result.

> *Often to keep a farm available for agricultural use, there must be a set of instructions, an agreement between owners and users, that define management, income and equity rights in property.*

For example, when you transfer land in your will, you often transfer the rights to income, management and equity to several people in equal shares. However, the rights in the income and management, while legally defined as equal rights, are nonetheless ambiguous between the new owners. Three people may have the right to manage the property, but what if they disagree? All have the right to income, but can all agree (and contribute equally) to the production of that income?

Often to keep a farm available for agricultural use, there must be a set of instructions, say in a trust or an agreement between owners, that define management, income and equity rights in property. Sometimes this can be a lease, sometimes a business entity such as a limited liability company, whose operating agreement clearly defines all the owners' rights to income, management and equity.

It is helpful to remember that regardless of the differing tax treatments, management and reporting requirements of business entities, all are essentially a contract between owners that describes, often in great detail, the rights of all owners in the income, the management, and the equity of the property that is owned by the entity. The agreement also prescribes the reaction or options in the event of a risk event occurring. Care must be taken to make sure your advisers fully understand your desires, values and risks.

In sum, to ensure your vision for the future of your farm as working assets, you will have to form an agreement with those to whom you entrust that future. As noted earlier in this workbook, it is a process to get agreements in place, and process to continually monitor them and change them when needed. It is a series of transactions that occur in a flexible framework that reflects your vision for the future.

Basic Estate Planning Documents: Wills, Trusts, and Gifting

Most families will transfer their wealth through their estate plans. An estate plan is a set of documents that clearly identifies who - and often under what terms - a successor will inherit property. Often, certain transactions will occur that can be referred to as 'estate planning' in the form of gifts or planned sales or other transfers in rights to property. The following narrative is a discussion of the nature of these documents and transactions.

The Will

Often referred to as your "last will and testament" a will is a document executed according to specific legal requirements that directs the distribution of your assets. The goal of any such document is to clearly express the intent of the person who makes it or directs its preparation and have it executed according to the requirements of state law, so that after your death anyone who disagrees with your distribution decisions will have a harder time trying to undo them.

In order to create a will you must be competent enough to know the nature and extent of your estate and be able to formulate a plan of distribution. A will must also be signed by you as "the testator" and signed by two competent and disinterested witnesses. These witnesses must be older than 18 years and must not benefit directly or indirectly under the terms of your will, and they must both sign in your presence and the presence of each other, all in front of an officer authorized to take oaths under state law, usually a notary public.

To change the terms of your will, any amendments or changes - known as a codicil - must be made with the same formality required of a will. Handwritten modifications to a will have no effect, absent certain legal formalities. You can revoke your will by executing a new will and stating in the document that you are revoking any previous wills.

Dying without a Will

You will often hear it said that there is no such thing as "no estate plan." If you do not have a properly executed - and therefore valid - will, the Revised Code of Washington has a plan for the distribution of your property and farm business assets. The intestate distribution scheme under state law covers exhaustive scenarios based on who is living and not living at the time of your death. Suffice it to say, if you plan to keep land interests in the family or pass a farm business within the family or to someone else, the ownership diffusion of intestate succession on the farm assets makes it highly unlikely that your farm will pass intact.

Can you disinherit your family in your will?

If a surviving spouse is not happy with property given by will, in some states the spouse can elect to take against the will and take the statutory amount instead. Most states provide that the surviving spouse can elect to receive a share of the decedent's total net assets if there are no surviving lineal descendants of the decedent. This is not the case in Washington, where a spouse has only a limited right to request a court award of a deceased spouse's property.

In Washington, there is a statutory provision protecting disinherited children if they are simply left out of a will. It is advisable to clearly state one's intent to disinherit a spouse or child to avoid a challenge. The Washington approach makes it far more difficult for disinherited children to challenge a will. Issues concerning undue influence or fraud, or improper execution of a will are more likely challenges if supported in the facts.

What will happen to my estate after I die?

The probate process is the legal process for proving the validity of a will and distributing your assets according to that will. The person who is named in the will as executor will be in charge of the probate process. The process can be lengthy and costly and usually lasts several months. With the supervision of the county clerk of court or probate clerk, the executor must identify and inventory property of the deceased, have the property appraised, pay all debts and taxes and finally distribute the remaining property as the will directs. If you die intestate (without a will), the same process will take place except the court will appoint an administrator of its choosing to carry out the probate process and the remaining property will be distributed according to state law instead of as directed by a will.

Probate is a public process and the proceedings will be available in public records. The property is often tied up in the process for several months or sometimes years and so will not be readily available to the heirs. For these reasons, many people try to avoid extensive probate proceedings. As mentioned above, property held in living trusts, joint bank accounts or pay on death accounts, real estate held in joint tenancy, and some life insurance proceeds are not subject to probate. However, it is strongly advised you take the time to understand how these alternatives may or may not fit by seeking the advice of a legal professional. For example, sometimes probate may be necessary to get real property titled in the name(s) of the proper successor(s).

Trusts

A trust is a legal entity that separates the management of property from the enjoyment of property. A settlor (aka grantor or "trustmaker") is the creator of the trust, and may also be the trustee who administers it and the beneficiary who enjoys it as is generally the case with revocable living trusts (i.e. created by a living settlor.) It all depends on the design of the trust.

The settlor transfers title of his or her assets (or "their" assets if a married joint trust) into the name of the trust, a process called "funding" the trust. This property, which is held in trust, is called corpus, principal or the trust estate. A trust instrument is the set of documents creating and detailing the terms of the trust. The instrument names a trustee to manage the trust property and often a backup trustee. It also names the beneficiaries who will receive proceeds from the trust during the life of the trust and the beneficiaries who will receive the corpus when the trust is dissolved.

Reasons for establishing trusts include: to avoid or minimize probate costs, to guard against will contests, protect privacy in property transfers, protect assets from risks associated with beneficiaries, allow for someone else to manage your property when you no long wish to or in the case you are no longer able to, allow someone else to manage property for minors, and in some cases to save estate tax. Trust options today are only limited by the creativity of the settlors and may serve very different purposes depending on the terms. Outlined below are several of the more common types of trusts.

Revocable Trusts

A revocable living trust is created by the settlor during their lifetime for their benefit. The settlor retains the power to destroy (revoke) the trust at any time during their life. Only at the death of the settlor does the trust become permanent (irrevocable).

A revocable living trust is sometimes referred to as a substitute for a will because its main purpose is to avoid probate of trust assets. Probate is avoided because the assets are no longer property of the deceased, but are owned by the trust – even though the deceased may have been both the trustee and the beneficiary. These trusts are particularly useful when property is held in several states which would require a probate in each respective state. Although probate costs are avoided, trusts usually cost more to create than a will because they are much more complicated to draft and fees may be associated with changing the title of assets. In addition to avoiding probate, trusts are less susceptible to attack than a will, because trust law comes from a different part of our legal heritage (equity law) and usually the trust has been in existence for some time before death. The court accepts the fact that the settlor could have changed the terms of the trust during their lifetime as proof that the trust is designed to accomplish their express intent.

Because the settlor retains control of the assets during life (settlor retains the power to revoke the trust and have the property returned), the property remains part of the taxable estate. Revocable living trusts are not useful for reducing the value of the estate for estate tax planning purposes, except for enabling spouses to split their estates to keep the value of their separate estates under the applicable exclusion (i.e. death tax exemption.) Washington currently has a $2 million death tax exemption per person, while the federal exemption has a base of $5,340,000 per person as of 2014, so careful planning is required to preserve and utilize each spouse' exemption in a marital community.

Revocable living trusts should be used in conjunction with a "pour over will". Since a will directs the court how to dispose of your assets at death, this provision will act as a catch-all and direct property still titled under your name to "pour" into the trust, normally to take advantage of an estate tax exemption of the first spouse to die. It also would nominate guardians for minor children. Additionally, durable powers of attorney for financial decisions and a number of health care legal documents should be included to complete the overall plan similar to a will-based plan.

Irrevocable Trusts
An irrevocable intervivos trust is a trust created during life that cannot generally be terminated or changed by the settlor once created. If created and managed correctly, these trusts can reduce the value of the taxable estate. The property will not be included in the value of the settlor's estate only if the settlor has severed his or her "ownership" and "control" of the property. It is critical to avoid tax inclusion in the settlor's estate that the settlor does not retain any interest in the income or corpus of the trust; it must benefit others. Additionally, the settlor cannot retain the power to change beneficial interests or the conditions of transferring the property or the property will be included in the settlor's taxable estate. One common use of irrevocable trusts is to own life insurance policies outside of the taxable estate. Most people are unaware that life insurance proceeds are normally part of your taxable estate. They are not income taxable to the person receiving proceeds at death, but they are part of the decedent's taxable estate!

Transferring property into an irrevocable trust is considered a gift to the beneficiaries and transfers may be subject to gift tax. Annual amounts over the current annual gift exemption transferred into the trust will be subject to gift tax. Under current law, an election can be made to transfer up to $5,340,000 million (subject to annual inflation adjustment) into the trust without paying gift tax; however, the transfer will reduce the unified credit and increase the amount of your estate that will be subject to estate tax at death. For very large estates, it may be valuable to make the election so that property appreciates in the trust instead of in the estate. Since the property must be forfeited by the settlor, the beneficiaries must have a present interest in the trust property.

Other types of trusts include testamentary or pour over trusts which are established by will. Spendthrift trusts protect assets which may be recklessly spent by beneficiaries, by limiting the rights of the beneficiary to sell or spend the trust corpus or principal. A Qualified Terminable Interest Trust (QTIP) provides a surviving spouse income during his or her lifetime. Charitable remainder trusts allows the settlor to contribute their property to charity and receive the income from the property over their lifetime. Special Needs Trusts can protect a disabled or elderly individual's qualification for supplemental security income, Medicaid, or certain Veteran's benefit programs.

Consequences of creating a trust including managerial capabilities, tax advantages and disadvantages, and revocability will vary greatly depending your specific circumstances. Consult with your attorney for more details.

Other trusts are *Charitable remainder trusts* that allow the settlor to contribute their property to a qualified charity and then receive the income from the property during their lifetime, with the charity receiving the assets upon you death. *Special Needs Trusts* can protect a disabled or elderly individual's qualification for supplemental security income or medicaid.

Gifting
The gifting of assets to the next generation before your death may be useful to decrease the size of very large taxable estates or to pass farm assets to a farm successor. There are several tax and other issues to be aware of when considering transferring assets by gift.

A gift of property is made only when you (the donor) exhibit the intent to give the property and there is actual or constructive receipt of the gift by the recipient (the donee). If property is of a nature that cannot actually be moved into the possession of the recipient, there must be what's known as constructive delivery. Constructive delivery is some action or transfer that gives the recipient the power to control the item received. Thus, a promise to make a gift, as in "All this farm equipment will be yours someday," does not satisfy the requirements of a gift. The farm equipment is still owned by you, and will become part of your estate if you do not otherwise dispose of it before you die.

Gifts must be given free of any restrictions and cannot be taken back at your request. In other words, you must be ready to completely part with the property and all its benefits (ie. use, income, etc.). For example, Dad gives Son his farm equipment but continues to use the farm equipment. This may be alright, but Dad uses the equipment under Son's permission. To eliminate any future questions by other heirs, tax authorities, etc., Dad should write up a list of the farm equipment and how much each item is worth, and attach it to a writing that clearly expresses his intent to give away the equipment with no strings attached. The son should sign the document to indicate he is aware of the gift, demonstrating his constructive receipt of the property.

Parents will often gift land to their children. There are tax consequences to such gifts (see below), but otherwise it is an effective way to transfer real estate. Once the land is gifted, however, the parents no longer have the right to receive rent from the property, so they should make sure that they have other sources of income for their later years. Parents sometimes find that gifting land gives them a piece of mind and the satisfaction of handing over a deed and witnessing the recipient's gratitude. However, although this may count as a gift, the recipient should record the deed immediately to ensure they take title to the property.

Tax Implications of Gifting

The gifting of property is not without tax implications. First, you can plan to gift property under your federal annual gift tax exclusion. In 2014, the annual exclusion amount is $14,000. This means that any one donor can make a gift of $14,000 to a single recipient without filing a gift tax return, and without deducting from their lifetime unified credit (amount of your estate excluded from estate tax) $5,340,000. Husbands and wives can combine their annual exclusion and give any recipient an annual tax-free gift of $28,000. Gifts can be made in these amounts to as many donors as you choose. Gifts for payment of educational and medical expenses are tax exempt.

Gifts in any amount are excluded from the recipient's gross income for tax purposes. However, if the recipient decides to sell gifted property there may be capital gains taxes. When a donor gifts an item to the donee, the donee receives the donor's basis in that property. Generally, "basis" is your cost of acquiring property plus the cost of improvements less cumulative depreciation. If the donee sells the gifted property, the donee will pay a capital gain on the difference between the sale price and the basis. (If an heir receives an asset at death by will or living revocable trust instead of during the life of the donor, they will receive a "stepped up basis" which is equal to the fair market value at the time of death.) The capital gain is an issue for the donee, and when offering a gift you might alert them to the choice of receiving the gift now with the carry-over basis, or waiting to receive the gift at your death (where they take the risk that you will have sold it or gifted to someone else in the meantime).

Many families have traditionally gifted partial interests in land by deed to their children, whereby the deed transfers, by way of example, a 1/64th interest in the property. It may be best to avoid such gifts as they create co-tenancies in land which may be hard to sort out later. An alternative is for families to place land in an entity such as a limited liability company, then gift interests in the company that fall under the annual exclusion. The interests in the real property, while not free of the carry-over basis issue, are nonetheless governed by the limited liability company's operating agreement, which grants options for ensuring that land can be controlled by the owners of the entity and stay in the family and available for farming use.

About the Federal Estate and Gift Tax: A 2014 Update

A concern in farm transfer planning for many years has been the federal estate tax. Since 2001, the federal estate tax has had an expiration date, where at some point in the future, the current relatively high estate and gift tax exemption would revert to a much lower exemption, potentially exposing your estate to taxation. At the very close of 2012, Congress passed the American Taxpayer Relief Act that established an estate tax regime that for the first time in over a decade did not have an expiration date. However, though many call the new law "permanent," it is nonetheless subject to change should Congress later decide.

The basics of estate and gift taxation are this: the totality of your wealth is subject to taxation at your death, unless its disposition qualifies as a deduction from taxation (ie. you transfer it to your spouse), or your total estate falls below a certain threshold amount, known as the *estate tax exemption*. No tax is paid on each dollar below that threshold, but for every dollar above that threshold a tax is paid based on a percentage calculated according to the size of your estate (your "bracket").

Likewise, gifts made during your lifetime are also subject to taxation, but no tax is paid by the donee so long as the gifts during your lifetime do not exceed a certain threshold. This threshold is your lifetime *gift tax exemption*, and it is the same figure as your estate tax exemption. In fact, this is a unified exemption: every dollar you use of your lifetime gift exemption is deducted from your deathtime estate tax exemption. Each individual also has an annual exclusion, whereby you can give gifts in a single year totaling a value that falls below a certain amount without deducting from your lifetime exemption (see below for amounts). For annual gifts of a total larger than that amount, the donor is required to file a gift tax return for that year, thus alerting the Internal Revenue Service that something must be deducted from their estate tax exemption.

2014 Federal Estate and Gift Tax Overview

What follows is a simple summary of the key components of the law for 2014 and beyond. The figures are scheduled to rise with inflation over the years, unless Congress again changes the law.

1) Estates worth $5,340,000 or less are excluded from the estate tax. Thus, if your estate is worth less than $5,340,000, your estate will not owe a federal estate tax.

2) Estates worth over $5,340,000 will be taxed at top a rate of 40%. The 40% tax rate only applies to the amount of the estate that is greater than $5,340,000. For example, if your estate is worth $6,340,000, an estate tax would be calculated on $1,000,000 of that amount.

3) Using the "portability of exclusion" rule, married couples are allowed to exclude up to $10,680,000 from the estate tax. Under this rule, each spouse can exclude up to $5,340,000. If the first spouse does not use all of his or her exclusion, the surviving spouse can add the remainder to his or her estate. It is not automatic: the surviving spouse must file Form 706 to capture this "portability."

4) The lifetime gift exemption is $5,340,000, which is tied to the estate tax exemption. Any gift that is made within an individual's lifetime in excess of the annual gift exclusion ($14,000) is deducted from his or her estate tax exemption. Thus, if you gift $1,000,000 in 2014, your remaining estate and gift tax exemption will then be $4,264,000 ($1,000,000 - 14,000 = 986,000; $5,340,000 - 986,000 = $4,354,000)

5) Individuals who distribute assets to a generation beyond their children (ie. directly to their grandchildren) will be exempt from the generation skipping tax (GST) if the transfer is less than $5,340,000. The top tax rate on amounts that exceed $5,340,000 is 40%.

6) Appreciated property in an estate can receive a step up in basis.

Entity Choice for Farm Enterprise and Farm Transfer Planning

One of the most common questions encountered when engaging farmers on transfer planning is about business entities, and their effectiveness in limiting operating liability (i.e. protecting assets from lawsuits and creditors). Placing land and operating assets into business entities is also an effective tool in transferring income, management and ownership/ control of those assets to ensure they remain productive or under ownership of the family.

Choosing a form of business entity is an important task that requires consideration of numerous issues specific to your goals. Concerns about entity choice typically focus on tax or tort liability. Though important, there are other critical issues that should not be overlooked. Issues such as management of the business, whether the activity is even a business (i.e., motivated by a profit motive), business continuity, transfer of land interests, and the need to attract outside capital often override tax and liability issues.

Some business entities exist by default, or by operation of law based on the circumstances of the endeavor. Others must be created by a filing with the Commonwealth, and then managed according to either the law authorizing the entity, or a more specific contract between the owners. Below is a discussion on the various types of entities, ranging generally from the simplest to the more complex. In reality, with the advent of limited liability companies (see below), some of the entities below have become less favored except under very specific circumstances.

Sole proprietorship

The sole proprietorship is not really considered an “entity,” it is just you trying to earn a profit in your business activity. Nothing is needed to create one although there may be a need in some cities and counties to apply for a business license. The owner of a sole proprietorship has the widest possible latitude to operate the business, and may do anything that is not prohibited by law. However, the sole proprietor retains unlimited personal liability, meaning all assets owned by the sole proprietor, even those not considered part of the “business”, are subject to the claims of others.

Partnerships

General partnership

A partnership is an association of two or more persons to conduct a business for profit. The relationship is consensual and often contractual. Like many other states, Washington has adopted the Uniform Partnership Act (UPA). Under the UPA, the partners must have equal management authority and share equally in profits and losses. They have an equal obligation to contribute their time, energy and skill without compensation to the partnership business. Each partner has unlimited personal liability to the creditors of the partnership, and all partners are liable for wrongful acts and breaches of trust by any partner. In other words, your personal assets are liable to claims that arise from the actions of your partner, even if that partner has not contributed property to the partnership (see discussion on unintended partnerships below).

A partnership files a federal information tax return (Form 1065) annually. However, all income flows through the partnership and is taxed to the individual partners. Each individual partners share of income is shown on a Schedule K-1 issued by the partnership. Each partnership interest is personal to the partner. Under UPA, partnerships are dissolved by the death of a partner or by the sale of a partnership share. However, most provisions of the UPA can be modified in a written partnership agreement. Such items that are typically modified include acknowledgment of differing capital contributions, different management responsibilities, unequal sharing of profits and losses, rights and obligations, and the terms of property ownership, termination and dissolution. Many such agreements contain a buy/sell agreement to address the situation when a partner wants to exit the partnership.

General partnership agreements may be oral, and are then governed by UPA. Furthermore, two individual sole proprietors cooperating their assets and efforts in a business can be considered a partnership by default, and therefore subject to UPA. In other words, courts can impose a partnership relationship upon parties who did not think that they were partners. Examples of relationships that may, in actuality, be partnerships can include employer/employee relationships, particularly where the employee has received a share of the crop and has shared in the risk of production; and landlord/tenant relationships, particularly those involving share-lease arrangements that are not in writing. .

Limited partnership
A limited partnership is a partnership whereby certain partners enjoy limited liability. This form of entity can be used when some partners want neither management responsibility nor the unlimited liability for actions of the other partners. Washington has adopted the Uniform Limited Partnership Act. Under this Act, a limited partnership is formed by at least one general partner and one or more limited partners. The general partner typically manages the partnership and has full personal liability for the debts of the partnership. The limited partner (or partners) contributes cash or other property only. The limited partner's liability for partnership debts is limited to the amount of his or her investment in the partnership. Limited partners do not participate in the management of the partnership. A limited partnership also files an information tax return, but income is taxed to the individual partners. Unlike general partnerships, limited partnerships do not exist by default, and must be created by a filing with the Secretary of State, accompanied by the required filing fee. A limited partnership is required to file an annual report for continued recognition under Commonwealth law.

A *family limited partnership* is a type of limited partnership used to promote efficient management of family businesses, business succession, estate tax management, as well as other purposes. Family limited partnerships are created the same as other limited partnerships and have the same filing requirements.

Limited liability partnerships
A limited liability partnership (LLP) is a general partnership that files an election with the Secretary of State. Such filing provides general partners with limited liability.

Limited Liability Company (LLC)
The LLC is a distinct entity that is a hybrid of a partnership and a corporation. An LLC is very similar to a limited partnership, only without the general partner who is required to accept unlimited liability. Owners of an LLC are referred to as "members." Those with management and decision-making authority are referred to as "managers." Like a corporation, the members have limited liability for debts of the LLC. Ownership and management of an LLC is governed by an operating agreement between the owners. The operating agreement can address any number of issues, such as division of profits between members, the limits of management authority without a vote of the members, and restrictions on who can become members as well as restrictions on transfers of ownership. LLCs are often used in farm transfer planning for a number of reasons. They can be an efficient way to manage and transfer assets over time to the next generation as a valued percentage of the entity as opposed to re-titling of individual assets. They can also restrict ownership of the entity to lineal family members. LLCs can be used both for management of farm operations and as land-holding entities. Land interests transferred to the ownership of an LLC lose certain attributes of real property under state law, and are treated as personal property interests governed by the operating agreement.

Corporations
A corporation is a legal entity, created under state law, that has rights and liabilities separate from its owners, which are called shareholders. A shareholder's liability for the debts of the corporation are limited to his or her investment in the corporation. The shareholders elect a board of directors who set the governing parameters of the corporation, known as bylaws, and appoint officers to manage the company on a daily basis. Normally shareholders do not participate directly in management decisions (unless they are also directors and officers). A corporation has a potentially unlimited life, and it is not automatically (by state law) dissolved by the death of a shareholder, director or officer.

Though shares of stock are freely transferable by the stockholder, smaller corporations such as farm operations can place limits on their transfer. Commonwealth law allows the creation of restrictions on stock transfers under the articles of incorporation, bylaws, or an agreement between shareholders and the corporation. One type of restriction would be a buy-sell agreement between a stockholder and the corporation or other stockholders requiring the selling stockholder to offer his stock first to the other party to the agreement. The agreement could set a price to be paid for the shares or a method by which they are to be valued, considering the shares were not publicly traded.

Shares in a corporation can be defined as *common* or *preferred*, based on the rights and privileges that belong to the owner. Common stock represents a fractional proprietary interest in the assets and good will of a corporation. Therefore, the common shareholder participates on a pro rata distribution of corporate assets upon dissolution, participation in corporate profits (dividends) and management of corporate activities (right to elect members of the board of directors). Holders of *preferred* stock are not creditors of the corporation and therefore do not share in corporate assets upon dissolution. Instead, they are first in line to receive fixed dividends ahead of the holders of common stock, and can have preferred rights ahead of holders of common stock with regard to distributions of corporate dissolution proceeds.

The shareholders are the actual owners of the corporation, and they choose the people who will manage the company, known as the board of directors. The shareholders elect the board of directors to delegate the power of management. The board is responsible for all of the business affairs of the corporation, such as issuing shares of stock and the rights of the shares issued, the sale of corporate assets, mortgaging corporate assets, declaring dividends, and the election of corporate officers. The senior manager of the company, often known as the Chief Executive Officer (CEO) and others that may comprise a senior management team are responsible for the day-to-day operations of the corporation. Their authority and duties are prescribed by the bylaws and the votes of directors, which are also governed by the bylaws.

A corporation is created upon the filing of the articles of incorporation with the secretary of state. This can be done on a form found online with the Washington Department of State, or can be more expansive document. Washington state law requires that the articles of incorporation include the following information: (1) a corporate name which must be available for use (ie. not being used by another corporation), (2) the number of shares that may be issued or whether the corporation is organized under a non-stock basis, (3) the street address and mailing address, including county, of the initial registered office (a P.O. box is not accepted), and (4) the name and address of each incorporator. Though not required, the articles of incorporation document may also provide: (1) the names and addresses of the initial board of directors, (2) provisions regarding the business purpose and par value of shares, etc., and (3) limitations on personal liability of directors.

At the organizational meeting of the corporation, bylaws should be adopted. This document may contain provisions for managing the company and regulating the affairs of the company that are legal and consistent with the articles of incorporation. The bylaws are the continuing set of governing rules under which the corporation, its officers, directors and shareholders exercise management powers, transfer shares, hold meetings and all other activities related to the corporate objective. The bylaws can be amended from time to time.

A business corporation can be dissolved in one of two ways: voluntary dissolution and involuntary dissolution. The directors and shareholders may voluntarily dissolve a corporation by passing a resolution of dissolution and filing articles of dissolution with the Secretary of State. Alternatively, a corporation can be dissolved without its consent by court action or administrative action of the Secretary of State. Such “administrative dissolution” can occur of the corporate managers neglect to file the required annual report and pay any associated fee with the department of state. Also, if the directors are not acting in the best interest of the company, any shareholder may obtain judicial dissolution.

C Corporations and S Corporations

A corporation can elect to be taxed in one of two ways under federal law. The corporation can elect to pay a corporate tax as an entity on its profits, with the shareholders paying a tax on their dividends. This is the famous “double taxation” we often hear about. Such a corporation is known as a “C Corporation” has elected to be taxed under Subchapter C of the Internal Revenue Code (IRC).

A corporation formed under Subchapter S of the IRC is a close corporation that has elected to be taxed like a partnership. Thus, instead of being taxed at the corporation level, the income is deemed to “pass through” to the shareholders and is only taxed once, at the individual level (whether the profits are distributed or not).

Corporations can also be not-for-profit, whereby all revenues are used by the business for charitable purposes. Non-profit corporations must apply for non-profit status with the Internal Revenue Service by filing a Form 1023 and paying the associated fee. Great care must be taken in completing this form, as IRS scrutiny of allowing non-profit status has increased in recent times.

Cooperatives

Cooperatives are another type of entity that has traditionally been used by groups of farmers to reduce the costs of inputs or to better pool and market products. Most cooperatives are organized as corporations; however, ownership of shares is restricted to the customers of the business. Profits of a cooperative are all eventually distributed to the members, after some is kept for administration of the cooperative. The cooperative itself is not designed to make a profit. The U.S. Department of Agricultural provides both technical and financial assistance to farmers who wish to form cooperatives.

Observing the Formalities

It is quite common for a family to prepare documents, file papers and then never fund the entities created. Oftentimes, attorneys that create the entities for the client fail follow up with their clients to ensure that the entities are being properly managed. Such management is required to demonstrate the continuing "business purpose" of the entity, to ensure that its limited liability holds up under the scrutiny of creditors and claimants.

Observation of formalities of entity maintenance such as holding necessary meetings and keeping minutes of those meetings must be strictly followed if the benefits of forming the entity that were hoped for are to be actually achieved. All required filings must be made and fees and taxes paid to avoid involuntary dissolution of the entity.

What is a buy-sell agreement?

A buy-sell agreement is a contract creating an option for one business owner to buy all or a portion of the business (which includes its assets) upon the retirement, death, divorce or disability of another business owner. Such agreements are often found as clauses in the governing documents of business entities such as partnerships and limited liability companies to restrict ownership of business interests. Sometimes they are stand-alone documents added later to an existing business by agreement of the owners.

The buy-sell agreement specifies who can buy the ownership interest, how the purchase price will be set and paid and at what interest rate. Terms of the sale and when the sale will occur are also included. Funding of the purchase can be an important consideration in drafting an agreement, and is usually accomplished with business cash flow, loans, life insurance proceeds or through the sale of other assets.

A buy-sell agreement allows the owners of business interests to agree ahead of time how to establish the value of the company and the value of ownership interests in a mutually beneficial agreement for all owners and their families. Such agreement helps to reduce uncertainty about what happens in the event tragedy befalls an owner. The agreement minimizes disruptions to the business operations after an owner's exit because the general circumstances of the exit have been contemplated ahead of time by all parties in interest.

Planning for the future of a farm in this way assures the business's stability and continuity and provides investment-decision stability for the purchasing owner and perhaps other key employees. If the buy-sell agreement covers land, it manages the risk that others - such as off-farm heirs - may gain an ownership interest and have different ideas about the use or disposition (ie. sale) of the land. In this form it is sometimes used to allow other heirs to participate in the equity of the land without ultimate control over disposition.

A common form of buy-sell agreement in limited liability company can work this way: One owner suffers a triggering event, such as death, a disability, files for divorce or files for bankruptcy, or a desire to leave the business. The agreement requires him or her (or his or her representative) to notify the other members in a specified manner, which starts a clock. The business itself may have the first option to purchase the business interests of the departing member. In the case of death of a member, the company may have purchased a life insurance policy on that member and the agreement may require that the company purchase the interest. In the absence of such requirement, if the business fails to exercise its option within the time period, the next option may fall to the remaining owners to purchase the shares, and if more than one steps forward, they can purchase a share commensurate with their then current percentage of ownership.

Agreements can identify future purchasers by name, which may be useful when a current user of the property - such as a farm successor on the farmland - needs assurance that he or she will have the resources to operate in the future, thus giving them confidence to continue investment in enterprises. Often this option is opened to the identified person's lineal descendants where it is important to keep land in the family.

An option holder usually has no right to force the sellers to give up their property, only the right to be the first in line to buy the property if the sellers decide to put the property on the market. The option holder cannot guarantee that the business interest will be put up for sale at a time where the option holder is able to cash flow the sale.

Rights of first refusal may also be written into a trust. Such an option would normally be triggered when a Trustee decides to sell a certain piece of property, such as land. If such an option is drafted into a trust, care should be taken to spell out how the price will be set along with the terms of sale. Trustees are bound by law to maximize the return to beneficiaries of the trust in the absence of any limiting language in the trust agreement. A specific person may be given the first option to purchase property from the trust of the deceased with the trust, and thus the beneficiaries, receiving the proceeds from the sale.

Though a buy-sell provision can make the use of entities a good option for families wishing to retain control of land, it is important to consider whether family members should be in business with each other, or whether it will be good for the family to create debtor/creditor relationships between them.

Worksheet 3.1

What's In An LLC Operating Agreement?

As you will note from the preceding article on business entities, a lot of decisions are required for constructing an agreement to meet your needs. A common form of business entity in farming and land ownership is the Limited Liability Company (LLC). An LLC is governed by a contract between the interest owners called an Operating Agreement, which covers many issues which are posed below as questions. Many if not most items in an operating agreement also have a default provision in Commonwealth law, but can be changed by agreement.

GENERAL CONSIDERATIONS	
State where entity will be formed	
Name of entity vs. trade name of business	
Cross check names with state Secretary of Corporations	
Narrative of business purpose (very important for farm LLCs)	
Term of entity (e.g. indefinite)	
Member-managed or Manager Managed (for LLCs)	
Identity of managers	
Agent and address for service of process	
CAPITAL CONTRIBUTIONS	
Initial capital contributions (and percentages) of each member	
Will members be required to make additional contributions if necessary?	
What happens if a member fails to make a required capital contribution?	
Who is allowed to become a member (e.g. lineal descendants of grandfather)	
What approvals are required to add new members?	
Are members allowed to withdraw their capital contributions? If so, under what circumstances?	
Is a member entitled to interest on his or her capital contributions?	
Does any member have any priority on distributions over any other members?	
INCOME AND TAX ALLOCATIONS	
How are profits and losses to be divided among the members?	
How are tax allocations made?	
When are distributions to be made?	

Should the agreement require special distributions to be made to at least pay for tax on each member’s pro rata income from the business?	
COMPENSATION OF MANAGERS	
What fees is the manager entitled to?	
What reimbursements is the manager entitled to?	
Is the manager entitled to incentive compensation?	
BOOKS, RECORDS, MINUTES	
What books and records are to be maintained by the business?	
What access rights will the members have to books and records?	
What reports will the members be required to receive?	
Who will be the tax matters partner?	
VOTING RIGHTS	
What voting rights will the members have?	
What major actions can the manager take without other members’ approval?	
Will a supermajority be required for some actions of the business?	
MEETINGS	
Where will meetings be held?	
How often will meetings be held?	
How can meetings (regular and special) be called?	
What notices for meetings must be given?	
What quorum is necessary for meetings?	
Can actions be taken by written consent of the members?	
ASSIGNMENT AND TRANSFER OF INTERESTS	
Do the members have the right to assign their interests in distributions?	
What rights does an assignee of a member’s interest get?	
In what situations will assignment be prohibited?	
What are the procedures for substitution of members?	
What happens on the death, incompetency or bankruptcy of a member?	

Is there a right of first offer or first refusal on transfers of interests?	
Are there restrictions on transfer of ownership interests? (i.e., owners can only be direct lineal descendents of grandma or grandpa)?	
Should a buy/sell agreement be included, setting out a formula to value ownership interests upon divorce, withdrawal of an owner, etc.?	
If included, should the buy/sell agreement include terms of payment for such business interests, allowing installment payments at a modest interest rate?	
Should key person life insurance provisions be included to fund purchases of a deceased owner's interest in the business?	
Should there be a prohibition on sale of ownership without permission of the other owners?	
REMOVAL OF A MANAGER	
Under what circumstances can the manager voluntarily withdraw as the manager of the business?	
What are the events that will result in the manager ceasing to be the manager of the business?	
Under what circumstances can the members remove the manager?	
What happens to the manager's interest when it has ceased to be the manager?	
DISSOLUTION AND TERMINATION	
Under what circumstances will the business be dissolved?	
Under what circumstances can the business continue notwithstanding a technical dissolution?	
How are distributions to be made on liquidation of the business?	
How can the business agreement be amended?	

Table 3.1

Quick Comparison of Business Entities

	Sole Proprietorship	General Partnership	Limited Partnership	Corporation	Limited Liability Company
Ownership	Single individual	2 or more general partners	1 or more general partners and 1 or more limited partners	1 or more shareholders	1 or more members
Direction and Control	Single individual	All partners	1 or more general partners and 1 or more limited partners	1 or more directors	1 or more members
Management	Single individual	Managing partner or all partners	1 or more general partners	1 or more officers	1 or more members
Liability	Owner has unlimited liability	Partners have unlimited personal liability	Limited for limited partners, unlimited personal liability for general partner	Limited	Limited or unlimited
Transferability	Not applicable	May be assigned, but assignee not a partner	May be assigned, but assignee not a partner	Corporate stock freely transferable, “S” corporation restrictions must be met	May be assigned, but assignee may or may not be a member
Continuity of Life	Terminates on owner’s death	Dissolves upon death or withdrawal, unless continued by partners	Generally dissolves upon death or withdrawal, unless otherwise specified in agreement	Perpetual	Operating Agreement determines continuity
Federal Taxation	Individual Taxed	Pass-thorugh entity (each partner taxed individually)	Pass-thorugh entity (each partner taxed individually)	“C” corporation and shareholders taxed; “S” pass-through entity, shareholders taxed	Pass-through entity (members taxed individually)
Legal and Administrative Costs	No initial or annual filings or fees or legal costs	No initial or annual filings or fees but may need legal service to draft partnership agreement	Initial and annual filings and fees, legal fees for drafting limited partnership agreement	Initial and annual filings and fees, legal fees for drafting documents, annual meetings	Initial and annual filings and fees, legal fees for structuring entity

Developing a Lease for the Farm

If you want to keep your land in farming, you will need someone to farm it. For most landowners, that will mean developing an agreement with a farmer for how the land will farmed. In Pennsylvania, land leases are governed by 68 P.A. §250.201 *et. seq.*

Many landlord and tenant arrangements have been based on family or neighbor relationships, and are often not in writing. In areas where farmers utilize fairly large tracts of land, rotating a limited number of commodity crops through the years, land is changing hands between generations which will likely change the way farmers and landowners have been doing business together. As more and more parents pass on, adult children inheriting rights in farms may want to hold on to them but are seeking a more formalized agreement with the farmer who has been tending the land. Closer to urban areas, some landowners who wish to hold on to the land for the foreseeable future may find opportunity in working with a farmer whose farming practices require a stronger tenure relationship than the traditional handshake. Even within families, a successor must often become a tenant before he or she becomes an owner of the land.

Guidelines for Landowners

There are several issues to consider before you enter into an agreement to create a successful working relationship with a farmer, either someone in your family, a neighbor, perhaps someone new to the area. For those landowners without experience renting or leasing land to a farmer, this narrative is meant to provide you with some of the basics involved with putting together an effective farmland lease agreement that will serve your needs. For those with experience, changes in agriculture practices and markets will likely bring up new issues you must address.

First, as emphasized in the previous section, you need to take stock of your land and take a look at what you have to offer and your goals for the property. For landowners, determining the amount and quality of land you have available is an obvious place to start. Keep in mind that not all land is created equal, particularly in the Southeast. Land usually slopes in one or more directions, it can be rolling and hard to see from all points. The key is knowing exactly how much land you have to work with.

Poor land, very small parcels, or land with poor accessibility and/or obstructions may not even be worth considering, as these may be too difficult to farm. Parcels too small to accommodate ever larger planting and harvesting equipment, yet remote from direct market opportunities may not be marketable for farming use. However, if the land is fertile, accessible, and of a decent size, you may find farmers interested in farming it. Indeed, in some areas you may be blessed with a healthy competition for leasing your land.

Landowners can turn to several sources to “discover” their land if indeed they do not already have a recent relationship with it. Many will have recreational relationships with their parents’ land (e.g. hunting, fishing or horseback riding), but may be less familiar with how it is managed for income production through farming or forestry. Landowners can inquire for their records through the county Farm Service Agency (FSA) office, which may include crop production history, aerial photos, NRCS program participation. Google Earth is a great way to get a recent aerial view of your land in great detail. Landowners can also request assistance from their county Cooperative Extension service who may have a working knowledge of how their particular parcel has been managed over the years, or the county Conservation District office, who might be available to walk the land and point out important soil and hydrological features, as well as certain restrictions pertaining to environmentally sensitive tracts of land.

Probably your best *first* person to help educate you about your land is the farmer who has farmed it. In many cases, this will help lay the foundation for a continuing, if more formalized, legal relationship.

As emphasized in Section One of this workbook, a clear statement of your values, goals and needs - as well as your desired role in decision-making - for your farm will form the foundation of your work on agreement with someone who will farm it, whether that person is related to you by blood or not. Below are a few points to consider from your side of the agreement:

1. **The written lease**: Lease agreements for farmland or other real property assets should be in writing. The

limited advantage of an oral, annual agreement is that the agreement ends at the close of the season. However, such arrangements create instability for both landowners and farmers. For landowners who will be providing more than just passive use of their land, such as providing lime, providing cash for custom tillage work from a neighboring farmer, or other inputs, you must protect your own liability by ensuring that the relationship with your tenant cannot be construed as a legal business partnership. Furthermore, you may wish to limit your own liability from practices of the farmer that may give rise to liability, such as misapplication of chemicals, environmental degradation, etc., and be sure that you are indemnified for any liabilities you may incur due to these actions.

2. **Ask questions**: Increase your understanding of how land is used. Understand that the language used by the farmer are those of his or her profession, terms that have everyday meaning to him or her will be unfamiliar to you. Do not be afraid that asking even a basic question will somehow expose ignorance and put you at a disadvantage in your discussions about a rental agreement.

3. **Be flexible (and clear) on your role**: In some cases, personal values that the land be farmed and well-taken care of will drive a landowner's desire to rent the land to a farmer. For those landowners particularly enthusiastic about emerging local food systems and environmental stewardship, you should be prepared that a farmer may have challenges with sharing daily operational decisions if you have no farming experience to offer. It may be best to consider your investment of land into this equation as your contribution, and defer to the skills of the producer in managing that contribution (again, subject to your goals, etc.). Even in share-lease situations, understand that a lease is not a partnership and should not give you the go ahead to weigh in on day to day decisions (unless you both have so agreed), this is a breeding ground for frustration and disagreement.

4. **Stay informed of market conditions**: This applies to both the market for land rents, as well as what is going on with either commodity prices or other product market conditions. Depending on the flexibility in your lease, or how you otherwise handle changed agricultural market conditions that affect the viability of your farmer tenant, you will need to be prepared to respond to the situation where the current rental rate agreement is jeopardizing the farmer's operational abilities.

5. **Schedule annual meetings**: Your ownership of your property should be considered a business, so you should have business-like meetings with your farm tenant to overview the season that has ended, issues that you want to bring up about the condition of the land, important changes in your life that will have an impact on the next year, particularly as they relate to your already stated goals for the farm. If there was something you saw that you were not happy with when you visited the farm, ask about it.

6. **Weigh new offers rationally**: Smooth working relationships between farmers and landowners can span generations. A stable farm tenant, when you consider your management options for the land, should be considered an asset. Be reasonable when offered a higher rent and improvements by a new and untested tenant, and allow your current tenant to address any issues where their work may appear deficient compared to what someone new is offering. In some areas, competition for land can be fierce, and though you may strive for a higher monetary return from the land, a revolving door of tenants may have its costs as well. Landowners should consider that, if not for this farmer and their stewardship of the land and relationship with their parents (which may have extended beyond mere payment of annual rent), they might have otherwise found the land in poor condition, eroded or grown up in unintentional trees of no commercial value.

General Guidelines for Tenants

For farmers, take a look at what *you* have to offer. Be clear about what type of farming you want to do on the land. You should be prepared to answer basic farming questions. Landowners - especially new purchasers or inheritors - may be extremely inquisitive about your farming practices simply because they may not be familiar with agriculture. Indeed, if you have been farming the land for a time, you may have had a fairly straightforward verbal rental arrangement with an elderly couple, perhaps a retired farmer, then his widow, now only to find that those who have inherited the land are raising new questions about production practices and rent. Farmers may consider that the inquiry may bring changes to how they have operated the land, and should be prepared to offer a basic and open education in farming practices. Remember that a little education will go a long way in creating a satisfying longer-term relationship with a supportive landowner.

The end goal for most farmers is a delicate combination of stability, affordability and flexibility. Many of the suggestions below for farmers are soft approaches, but experience has shown that solid relationships can sometimes transcend economic and competitive issues normally associated with how much rent you can pay for use of the property.

The following points should be included in the farmer/tenant's landholding strategy:

1. **Ask for a written lease**: Oral leases can provide opportunities for disagreement, even based on innocent misunderstandings, which once crops are planted become more difficult to resolve. Further, your investments in the land - such as a three-year lime application - are not protected under an annual oral lease, only your right to harvest planted crops is protected by state statute.

Clear language will resolve many issues, but a lease can also provide a dispute resolution scheme for when disagreements occur due to actions of either party during the lease. Further, should the land change hands during the term of the lease - due to death of the landlord or sale or gift of the property - a written lease offers protection to the farmer. Washington State require leases with a term exceeding two years to be recorded with the county Recorder's Office in order to warn purchasers of the land that there is a tenant with farming rights on the land. (Note: in order to protect the confidentiality of elements of the agreement, such as the rental rate, a Memorandum of Lease can be recorded to satisfy this requirement).

2. **Provide a resume**: When approaching landlords that you have not worked with before, you should provide an overview of your farming operation and experience, including philosophies on production practices, business objectives, education, tillage practices, equipment use, financial strength and other land tenure relationships. Some prospective landlords might not agree with your philosophies and practices, so it is good to know earlier as this will only cause problems in the arrangement as time moves forward, causing stress on the success of the operation.

3. **Agree on a cropping plan**: Open dialogue early on a cropping plan, which should include input and field operation specifics. For new and/or younger farmers interested in smaller-scale, high intensity production for direct market, be prepared to have your business plan ready for review. You must build this landowner's confidence in your ability to continue a business on their land.

4. **Keep communication open**: Providing regular updates on crop conditions, markets, and planned activities such as cropping and harvesting, conservation implementation (if authorized), general cattle rotations, etc. will help visiting landowners (who will sometimes visit the property in the farmer's absence) understand changes they are seeing on their property. A report can give you a baseline to refer to when asked later about something they have seen happening on their property. Consider including cost information in these communications, as this will help the landowner understand certain issues that may become relevant regarding rent amounts, landowner contributions (if applicable), etc. When on-farm problems occur, notify the landowner.

5. **Educate the landowner**: As noted above, just by virtue of time and rural demographic changes, more farmers will be working with more non-farmer and absentee landowners. To educate the landowner, the tenant may consider strategies such as regular mailings of farm journal articles or developing a website to educate the landowners and their potential heirs while demonstrating the farmer's interest in their knowledge. In some cases, particularly nearer to urban direct markets, it may be helpful to educate the landowner in how their land is part of a larger farming and food system, one in which they are a key player. Some inheritors of land, themselves urban dwellers with an interest in "local foods," express the interest that their land be farmed "organically" without understanding the technical nature of the term. Your ability to provide them with a bigger picture, while helping them understand the "technical" nature of organic production may serve you well.

6. **Improve the farm**: Experienced farmers often state a goal of leaving a farm in better shape when they got it. The farm's appearance - maintenance of roadways, fences, clearing brush around old houses and structures - is usually the first impression other landowners get of the farmer's reputation in the neighborhood, which will correlate directly to the perception formed on that farmer's abilities and value

as a tenant. Consider this a visual resume of your abilities.

7. **Pay attention to the current owner**: Acknowledging life events - holidays, birthdays, the passing of close relatives - of landlords improves a farm tenants longer term access to the ground. When receiving honors for conservation or other practices, it sends a strong message - if the venue is right - to also invite and recognize the landowners you work with.

8. **Don't forget about the future owners**: Land is going to change hands, in many cases sooner rather than later. This workbook encourages owners of land to engage their families (i.e. children or other potential heirs) if planning needs to be done for the future of the land. Farmers should look for ways to include the "next generation" owners where possible in their passive communications with the landowner while being sensitive to established lines of communication within the family.

Types of Leases

Cash Rent

Most rental arrangements are for a set price per acre for a set time, normally per year. The farmer pays the landowner the total of the rate per acre multiplied by the number of acres farmed. Under this arrangement the tenant bears most of the costs - and thus most of the risks - of preparing the land for production and growing and harvesting the crop. Thus, the tenant still owes rent in the event of crop or market failure. Some cash leases provide for an amount paid tied to the price of the crop, actual yields, or a combination of both, and can offer a lower base rent to protect the farmer in bad years while rewarding the landowner in better years.

Crop Share

A crop share risk allocates risk between landowner and tenant, splitting the costs and the proceeds of production according to agreement. Crop (or livestock) share leases allow landowners in strong financial position to contribute to costs of production, which can be of great help to a newer farmer shorter on early season operating capital. Care must be taken to distinguish such an arrangement from a legal partnership. Share leases can also give the landowner a specified share of the crop (which the farmer can buy for a set price or the landowner can sell on the open market), so when the farmer does well the landowner does well. (See sidebar *Comparison of Cash Rent and Crop Share Leases* next page)

Basic Elements of an agreement

Below are the very basic elements of a lease agreement. As alluded to earlier in this narrative, there are many variations of the themes below.

1. **Identity of the parties**. The lease must be signed by the actual owner(s) of the property or those with proper authority to bind the property to the terms of the lease. Keep in mind that property that has been inherited may have more than one owner. If property is held in a trust, the trustee must sign. If land is held in a limited liability company, the person with management authority must sign. Failure to secure the signatures of the proper owners leaves the lease vulnerable to being voided by owners who did not consent to the agreement.

2. **Description of property**. The property description in the agreement identifies the land both parties intend to be farmed. The lease should identify the land area, buildings, equipment and animals (if applicable). Land can be described by inserting appendices to the agreement (properly referenced in the document) that contain either the deed description or a portion thereof, and/or aerial photos of the property from FSA or county Geographic Information System (GIS) website or Google Earth, with fields and access marked on the photograph. If possible, land should be described by reference to a formal legal description even if the lease will only cover a portion of the legally-described property. Access should clearly be set out, especially where access crosses other land or to structures not in the leased premises..

3. **Term of lease**. The lease should specify when it begins and when it ends. In coming to an agreement, the farmer should consider the amount of time necessary to recoup his or her investments in the land. Multi-year leases can offer a set term that binds the property for that period, with a renewal clause that should be clear on how renewal takes place or notice of termination is given (i.e. time period and manner). It is reasonable to both parties to allow a minimum six-month period to announce an intent not to renew the lease. Any lease with a term exceeding two years should be recorded.

4. Amount and terms of rent. For a cash rent lease, the amount of rent is normally paid in one payment by a particular date, traditionally near the end of harvest when the farmer has cash from the sale of crops. For more diversified operations with earlier market harvests, the parties can agree to an installment schedule for preparation of the land, spring crop harvest and fall crop harvest. Determining a fair rate is often a challenge, but there are several methods to consider (see sidebar *Determining a Fair Rent, next page*).

5. Allowable and prohibited uses. The lease normally limits use to agricultural production. Some landowners may want to specify prohibited uses, such as chemical application. Landowners should consider the practicalities of limiting certain activities that would otherwise reduce the productivity of the operation. Remember that all prohibited uses can be qualified by written consent if the lease so declares. Below is a partial list of issues to address:

- The lease should address protection of conservation program features, including buffers and grass waterways.

- State and federal regulations and laws should be incorporated by reference. If the landowner will allow application of chemicals (pesticides,

Comparison of Cash Rent and Crop Share Leases

(from *Improving Your Farm Lease Contract*, Iowa State University)

Cash Lease

Advantages of a straight cash lease are:
- The lease is simple with relatively few chances for misunderstanding.
- The owner is relieved of making day-to-day operating decisions.
- The owner has very little financial risk.
- The tenant has maximum freedom in planning and developing the cropping and livestock programs.
- The tenant has fewer records to keep.

Disadvantages and potential problems of the straight cash lease are:
- A fair cash rental rate may have to be renegotiated each year.
- Cash rents are likely to be too low in times of rising prices and increasing yields, and too high in times of low prices or low yields.
- Tenants are required to supply more operating capital.
- Tenants bear all the risk of price and yield variability.

Crop-share Lease

The advantages of a crop-share lease are:
- Crop risks associated with price and yield variations are shared equally.
- The owner is more involved in operating decisions and marketing the grain during the year.
- Both parties share the benefits from adoption of yield-increasing technology, or unexpected high yields or prices.
- A second USDA payment limit is created.

Disadvantages or potential problem areas of a crop-share lease include:
- The landlord and tenant must determine how production expenses are shared.
- Adjustments for sharing costs for storage and drying facilities, herbicides that reduce field work, or fertilizer and pesticide application may have to be made.
- The cropping plan to be followed and whether or not the farm participates in government programs must be agreed on.
- Added cash rent for buildings and facilities may have to be negotiated.
- If the owner's and tenant's grain is stored in a common bin, marketing decisions have to be made jointly.
- The landowner may be considered a material participant, and farm income will be subject to self employment taxation.

DETERMINING A FAIR RENT

In a lease agreement, determining a fair price is often the most important factor for both parties, yet it can be difficult to establish in many farming situations. Location, soil quality, the forces of supply and demand, commodity and direct-market prices, as well as your personal goals for the land all play a part. For higher-grossing, larger acreage operations, establishing a rental rate can be more straightforward where there is a history (and reasonable forecast) of cost and price information.

Many landowners have traditionally charged just enough to cover the taxes on the land. Others don't charge, especially when the trade-off is keeping a pasture mowed (in exchange for the hay the farmer takes). Most agreements are set up on a per acre basis, where a rate per acre times total acreage used becomes the annual payment. Below are some considerations for setting the rental rate:

1. **Market rental rates**. The only practical way to determine real market rates is to ask around. As best as possible, talk with local farmers to get a feel for what they are paying for land. Call the cooperative extension office for the county: if your farm is in pasture, ask to speak with the livestock agent; if your farm is in row or field crops, ask to speak with the agent who advises farmers on those crops. If you are an "absentee landowner" (ie. you do not currently live in that community), be sensitive to the fact that you are inquiring about issues that may economically impact the businesses of farmers that local cooperative extension agents and soil & water conservationists have worked with for years. Remember that land and the infrastructure on it can vary greatly, so what others are charging may not be appropriate for particular farm. Make sure you compare your rate to rates for land of comparable quality, based on actual yields or productivity indices.[1]

2. **USDA Farm Service Agency (FSA) county average rental rate**. The USDA Agriculture Statistics Service surveys farmers and landowners to compile annual reports of average rents for high, medium and low productivity crop and pasture land. Note: The results of these surveys, while considered reliable, may not accurately describe conditions in certain parts of a county.

3. **Cost of land to the landowner**. Many landowners are content to simply cover their costs of "carrying" the land. These costs typically are the sum of depreciation (on certain structures), insurance, repairs, taxes, and interest. Most agricultural and horticultural land (and a fair amount of forested land) is enrolled in the state's "differential assessment" property tax program whereby qualifying land is assessed at a property tax rate lower than its highest use. The program normally requires that farm and horticulture land produce a set annual gross income, which can be quite low, but nonetheless requires someone to farm the land and show income receipts.

4. **Costs of production (Tenant's Residual)**. Another approach is to calculate how much income the tenant has available for rent payments after subtracting all the tenant's costs associated with producing the crop on the land. This approach will require yield estimates, projected market prices, and perhaps government payments, to determine an income picture. Next, calculate the operating expenses for the year. Next, subtract the tenant's cost of machinery and equipment ownership, which includes costs such as depreciation, a return on investment, insurance, and machinery housing. Finally, a figure should be calculated and subtracted for the tenant's labor and management. The remaining amount is available for the payment of cash rent. Without the willing participation of a prospective and experienced farm tenant, this approach will be a challenge for most landowners.

1 http://www.extension.iastate.edu/agdm/wholefarm/html/c2-20.html

herbicides, etc.) to be applied to the land (indeed essential to many production areas), the lease should state that only USDA approved chemicals be used and applied according to federal and state regulations. Further, the lease can restrict application of chemicals that have a residual life beyond the term of the lease.

- If the landowner intends to reserve mineral rights to the property, extraction activities such as removal of sand or gravel should also be expressly prohibited.

- It is prudent for the landowner to require the property to be left in the same condition as when the lease began, and include a redress for documented damages to the property (a photographic baseline can be made at the beginning of the lease). Though a prudent would-be tenant will have inspected the land, the soils and water availability before choosing to farm that property, the landowner should make clear that he or she offers no warranty as to the production capabilities of the land.

- Any land clearing should be discussed beforehand, and burning should be reserved to consent of the landowner upon showing of proper permits if applicable to the area.

6. **Repairs and maintenance and improvement costs.** Maintenance of property should be allocated between the parties, including responsibility for routine repairs and those caused by extreme weather events or fire. Be sure to list items such as fencing, gates, wells and pumps, etc. *See Worksheet 3.3: Repairs and Maintenance Checklist*. In many farm situations there are structures that the Tenant installs but intends to remove, such as hoop houses, moveable cattle fencing, etc. Be sure to identify in the lease that these are not fixtures and the Tenant will be removing them at the end or termination of the lease. Likewise, if items such as grain bins are anchored to cement pads and such, be sure to agree what happens to the bin and the padding at the end of the lease, whether it left in place or the Tenant must dig it up and repair the ground.

7. **Rights and obligations of both parties.** Issues that can be addressed can include prohibitions on the right to sublease, payment of utilities, right of entry and inspection by landowner. The lease should include a statement that the lease is not a partnership between landowner and tenant , as well as a statement binding the heirs and assigns (i.e., subsequent purchasers) to the terms of the lease agreement. The lease should also contain a clear indemnity clause, requiring parties to pay for liability attributed to one party for the actions of another. It is common sense to require that both parties keep insurance policies at a designated level for just such a purpose.

8. **Termination of the lease and default**. Default means that one of the parties has not lived up to the obligations attributed to them in the lease. Numerous events can trigger default: failure to pay rent, failure to abide by any use prohibitions, maintain liability insurance, comply with laws and regulations, bankruptcy, etc. Default does not necessarily trigger termination, but should trigger a process for recognizing and curing the default if possible. If the default cannot be cured, a process should be spelled out for repossession of the property by the landowner, including reserved rights to crops by the farmer. Disagreements should be subject to a clear dispute resolution process.

9. **Payment of property taxes and insurance**. Though many landowners might agree to a rental rate that covers their carrying costs (property taxes and insurance) on the land, be sure to spell out who has responsibility for these expenses (the landowner is responsible for taxes and ultimately insurance, but be sure they understand this or that you are agreeing to pay these over and above or in lieu of rent).

As a practical matter, a lease is only as good as the parties' willingness to enforce it in court. The more thorough and open the agreement process, the less likely a disagreement will occur in the first place. Although it is likely impossible to build a lease agreement that will provide for all contingencies that might occur, both parties should try to anticipate foreseeable occurrences and identify the procedure for what the parties do should something unforeseen occur. Because both landowner and farmer benefit from a written lease agreement, both should take care in developing an agreement that supports each other's goals.

Worksheet 3.2

Short-Term Lease Checklist

Use this worksheet to ensure key areas are addressed in your discussion of a lease agreement. Each item will require discussion between both parties and legal counsel.

1	Who are the parties? Make sure you have evidence of ownership and authority to act if the landowner is an entity (ie. LLC, estate, trust) other than an individual. Make sure the lease binds "heirs and assigns."
2	What will be the lease term? State law may require recording of the lease or memorandum in the register of deeds for the county where the land is located.
3	Will the lease be renewable? Will both parties have the option to renew or not renew? How much notice is required for renewal, and what is the procedure?
4	Do you have an adequate description of the property (real and personal) to be leased (land, boundaries, farm structures, residence, equipment, etc.)? If a good written description is elusive, include an FSA aerial photo with boundaries marked as an exhibit.
5	How much and what type of rent will be paid? When must the rent be paid? (see worksheet *Determining Rent*)
6	If the agreement includes a residence, will there be a separate residential lease?
7	What will be the allowable and prohibited uses of the property under the lease? If chemicals are allowed, who bears liability for their misuse?
8	How will the landowner and the tenant allocate responsibility for repairs and maintenance of the property? (see worksheet *Repairs and Maintenance*)
9	How will the landowner and tenant allocate responsibility for capital improvements? If the tenant invests in capital improvements, how will they be compensated?
10	Who will be responsible for obtaining and maintaining insurance - liability, casualty or crop insurance?
11	What actions by either party will constitute default under the lease? Will the non-defaulting party have the right to terminate the lease or withhold rent until the default is cured? Will the lease include a procedure for dispute resolution?

Worksheet adapted from *Holding Ground: A Guide to Northeast Farmland Tenure and Stewardship.*

Worksheet 3.3

Repairs and Maintenance Checklist

This worksheet can be used to support a clause in a lease agreement requiring that landowner and farmer will visit the issues of repair and maintenance on an annual basis. Each party should keep a copy.

Year: ______________				% of Cost Contributed by Landowner and Tenant				Total Dollars Contributed Toward Repair		Value of Labor	
				Materials		Labor					
	Repair or Replacement to be Undertaken	Date to be Completed	Estimated Cost of Materials and Labor	L	T	L	T	L	T	L	T
Structures: Exterior siding/ Windows/ Roofing											
Fences											
Barn Equipment											
Water, Heating, Ventilating Systems											
Waste Management Systems											
Conservation Structures											
Total											
Landowner (signed)				Farmer (signed)							
This worksheet adapted from USDA form AD 562 (Mar 1960)											

About Conservation Easements

Conservation Easements are a land "protection" tool authorized state law and recognized by Revised Code of Washington (RCW) and the Internal Revenue Code to protect and conserve land. Conservation easements are used to protect a variety of landscapes including farmland, forestland, ridgetops, historic structures, wetlands and beaches. They are a specific exception to the common law rule that one cannot create a perpetual restriction on the use of real property.

The utility of the conservation easement as an effective tool in your farm transfer planning depends on your goals and financial needs, but it should never be substituted for other estate planning documents such as a trust.

Because conservation easements are a relatively recent legal concept, many landowners are unfamiliar with their use and particulars. At its most basic level, a conservation easement allows a landowner to continue to own the land while placing certain voluntary restrictions on its current and future use. These restrictions can include limitations on subdivisions and development. In exchange for these restrictions, landowners can receive payment or tax benefits (or sometimes a combination of the two).

This narrative should answer basic questions that a landowner -- particularly of farm and forest land -- might have about conservation agreements, and whether they are something to explore further. Remember that a conservation easement is a real estate transfer of certain rights and interests, and should be seriously considered with the help of a legal and tax adviser experienced with such transactions.

WHAT IS A CONSERVATION EASEMENT?
A conservation easement is a written agreement between a landowner and a qualified private non-profit organization such as a land trust, or a county agricultural conservation easement program.

The conservation easement has two essential elements:

1. The landowner (grantor or donor) agrees to protect certain conservation values on the land, such as agricultural values, open space, scenic and historic resources, water quality, and wildlife habitat.

2. The conservation organization or public body (grantee) is granted the right to monitor the property and enforce the restrictions in perpetuity (forever). While the landowner may sell the land, the restrictions continue to apply to all future landowners.

Many folks often ask the question of whether a simple deed restriction can protect the conservation values of land. The key challenge is that there is no permanent mechanism of enforcing the terms of the conservation easement. The nature of a conservation easement is to grant a third party the right to ensure that the conservation (or working) values are not threatened by actions to the land, such as uses that negatively impact the conservation values of the property.

These type of restrictive easements can be called a number of names, including deed of conservation easement, a sale or grant of development rights,

Photo courtesy of Washington State University

a working forest easement and an agricultural conservation easement.

Conservation easements are intended to protect property from residential or non-farm commercial development, thus providing a benefit to the public by conserving open space vistas, making farmland available, protecting against water pollution from runoff, or protection of scarce natural resources such as wildlife habitat or rare species.

In exchange for this public benefit, there are sometimes funds available to pay for the diminution in property value caused by such restrictions, though in recent years of fiscal tightening these funds are less available. There can be significant federal, state, and local tax incentives for a landowner if he or she donates the right to enforce restrictions to a qualified organization. To qualify for these tax incentives, the terms of the conservation easement, though flexible, must conform to the regulatory requirements of these tax incentives, and any use exceptions -- particularly for farms and forests -- must not significantly diminish the land's "conservation values."

In general, a conservation easement can be a useful tool to landowners who a) have a strong desire, a core value, that the land not be further developed or used more intensively than at present (ie. in farming), and b) are able to utilize attendant tax deductions and credits.

Conservation Purposes

A key feature of a donated conservation easement to understand is that it is perpetual and does not expire or revert back to the landowner at some appointed time. You may hear people refer to this as "forever protected," which, though difficult to imagine, means that as long as an entity exists to enforce the terms of the conservation easement, it will protect the land. Some states, including Washington State, allow non-perpetual (or "term") conservation agreements. Though landowners will often be compensated for such agreements, these generally do not qualify for tax deductions or credits.

To qualify as a charitable contribution for federal tax purposes, a transfer of a conservation easement deed must be made to a qualified grantee (generally a nonprofit organization or a public agency). The deed must restrict the property to the point of meeting one or more of the following conservation purposes:

1. Protection of relatively natural habitats of fish, wildlife, or plants;

2. Preservation of open space including farm and forest land;

3. Preservation of land for public outdoor recreation or education;

4. Preservation of historically important land or buildings.

These conservation values must be established through a natural resource inventory that can include maps, photographs of existing buildings and roads, a description of natural habitats, and a survey of wildlife should be prepared. The inventory allows is known as the "baseline," and will be the reference point of the values that will be defined under the conservation easement. The owner can decide which conservation purpose is met by which part of the property, and can distinguish ecologically sensitive areas from other areas that might be appropriate for other uses.

Rights, Restrictions and Allowable Uses

A conservation easement's restrictions should be tailored to the particular conservation values of the land and interests of the landowner and grantee. Examples of activities that may be prohibited or restricted in a conservation easement include industrial use, mineral exploration or soil excavation, subdivision into smaller tracts, residential development, road and infrastructure expansion, and extensive timbering. Though a conservation easement may offer some protection through the public advocacy of the conservation easement holder, it is ultimately not effective against eminent domain.

Depending on the size and character of the land, conservation agreements may allow timbering and forest management and agricultural use. The conservation easement might also allow wildlife management, hunting and fishing, or even the construction and maintenance of a limited number of new homes or other infrastructure necessary to produce income from the property. Such improvements will often be limited to certain well delineated areas called "envelopes" which can be strictly enforced. (Note: moving building sites or amending the size of the parcel is very difficult later)

The grantor retains ownership along with the right to manage, care for, and derive income from the property. Conservation easements are not generally effective in imposing affirmative duties or obligations on the landowner. In special cases, as in the case of sensitive wildlife habitat, a conservation easement holder with a particular expertise may have the right to undertake certain management activities on the land. As discussed below, conservation easement may qualify the property for Current Use Tax Classification under Washington's Open Space Taxation Act,.

As noted, a core function of a conservation easement is to limit subdivision or otherwise prescribe how land can be subdivided into smaller tracts. Even so, the owner can still sell, encumber (mortgage) or otherwise convey the rights in the land through lease, will, trust, or to a management entity such as a limited liability company. However, the land remains subject to the conservation easement. The rights the owner retains pass to any heirs or assigns (by gift or sale).

With regard to using the land for security on a loan, the value of the land as collateral will be its restricted value, not its "highest and best use." The lower value primarily reflects its subdivision restriction, since smaller parcels are more marketable and can sell at higher prices. If there is an existing deed of trust securing a loan on the land, the lender will require that it be subordinated to the conservation easement.

When tax benefits are realized, the holder of the conservation easement is required by the Internal Revenue Service to monitor and enforce the obligations contained in the conservation easement Therefore, the conservation easement must provide for an annual visit by the conservation easement holder. The grantor and the grantee can decide for more visits, particularly if the conservation easement has motivations of habitat research.

Where the Grantor reserves rights, such as the right to timber or to subdivide, the conservation easement may require a review and approve the exercise of such rights by the grantee of the easement.

In most cases, a conservation easement does not require or allow entry by the public. Even conservation agreements that protect significant natural environmental systems, such as fish, wildlife, or plant habitat, or forestland and farmland, where there is an official government policy to protect forestland and family farms from fragmentation, will not require public access. However, sometimes scenic and open space easements require visual access to qualify for deductions under the Internal Revenue Code. These conservation easements are designed to protect the scenic character of the land, and thus the requirement that the land can be viewed by the public is critical to its conservation value.

Conservation Easement Tax Advantages

As noted above, there are tax advantages for the donor of a conservation easement. The tax implication is generally related to the value of what the donor is giving up, usually the right to subdivide and further develop the property. Several advantageous provisions for farmers expired 2011 but were reinstated in 2013, retroactive to the beginning of 2012.

Federal Income Tax

If the conservation agreement gift is made during the Donor's lifetime and the land is long-term capital gain property, the Donor may claim a federal income tax deduction for the full fair market value of the conservation agreement.

However, to prevent a Donor from using the deduction to avoid paying tax, the Internal Revenue Service (IRS) places a cap on the amount of the deduction that can be claimed in the year the donation is made. For 2014, the cap is currently set at 30% of the adjusted gross income for individuals. Individuals may carry over 30% of the unused portion of the donation for the next five years until the deduction is fully exhausted.

The Enhanced Conservation Easement Tax Deduction for farmers expired at the end of 2013, but may be renewed. Here is how the old law worked in case it is reinstated: Individuals that qualify as farmers by earning more than 50 percent of his or her income from "the trade or business of farming," the tax deduction is raised to 100% of adjusted gross income. Any unused deduction can carried forward for the fifteen years following the year the donation is made.

Below are activities that may count as farming:

- Cultivating the soil or raising or harvesting any agricultural or horticultural commodity (including raising, training, and management of animals) on a farm;

- Handling, drying, packing, grading, or storing on a farm any agricultural or horticultural commodity in its unmanufactured state, but only if the owner or operator regularly produces more than one-half of the commodity so treated; and

- Planting, cultivating, caring for, or cutting of trees, or the preparation (other than milling) of trees for market.

The easement in these circumstances must require the land remain "available for agriculture."

Federal Estate Tax
Conservation easements offer estate tax benefits, in that a conservation easement will generally decrease the land's fair market value due to development and subdivision restrictions. The restrictions will stall the rapid appreciation of the property tied to residential or commercial development potential for that property. The lower land value may serve to decrease the overall estate value that might otherwise be exposed to an estate tax.

Under the Internal Revenue Code, if certain requirements are satisfied, an executor can elect to exclude up to an additional 40% of the after-easement value of the land from a landowner's estate for estate tax purposes (subject to a $500,000 maximum).

However, be aware that, even with a conservation easement, land can still appreciate, and given the location and desirability, can appreciate higher than originally anticipated when the conservation easement is donated during one's lifetime as part of a comprehensive estate planning strategy.

If the conservation agreement is granted by will, the Donor's estate may claim an unlimited charitable deduction for the value of the agreement, which has the same effect of reducing the estate tax. In this case, the testator can have directed that an easement be donated upon his or her death, or can give the executor the power (option) to do so if it appears such donation will serve to retain wealth (ie. lower or eliminate estate tax burden). Up to $500,000 of the land's residual value may also be deducted from the value Donor's estate in some special situations.

Local Property Taxes
Washington's Open Space Taxation Act, enacted in 1970, allows property owners to have their open space, farm and agricultural, and timber lands valued at their current use rather than at their highest and best use. Because a conservation easement has the effect of reducing the fair market value of land, the taxable value of land subject to a conservation easement should be reduced accordingly, thus reducing the tax burden on the landowner.

VALUING CONSERVATION EASEMENTS FOR TAX PURPOSES
An appraiser uses a "before and after test" to determine the value of a conservation easement. Simply, the value of the property whose uses are restricted by the conservation easement is subtracted from the value of the property as if there were no conservation easement restrictions. The difference between the two appraisals is the value of the conservation easement.

Sometimes, the presence of a park or other conservation property can soften the reduction in value as it is an amenity to adjacent land, and actually results in added value to the adjoining land. This happens when the Donor or Donor's family owns the adjacent property that increases in value, whereby the appraiser must reduce the value of the donated conservation easement by the amount to which the other property increases in value.

An appraiser who understands the local real estate market and conservation easements should do the appraisal. When the motivation for donation is an income tax deduction, one would think there is an opportunity to substantially increase the deduction by dramatically lowering the value of the land under the conservation easement restrictions. However, there are substantial penalties imposed on both donors and appraisers for such overvaluations. Furthermore, the donor, appraiser, and the grantee organization must all sign a special tax form (Form 8283) in order for the donor to claim a federal income tax deduction.

THE CONSERVATION EASEMENT TRANSACTION
Conservation easements may be granted to public agencies, such as federal and state agencies, counties and towns, or to a nonprofit tax-exempt conservation

organization. An example of a public agency would be a county soil and water conservation district. A non-profit entity will normally be called a "land trust" or "conservancy."

Conservation easement transactions are complex. To ensure the conveyance of a conservation easement will qualify for a federal tax deduction, certain documents must be prepared, including:

1. *Deed of Conservation Easement*. This is the document that outlines the agreement, and whose language supports the public purposes that qualify for tax benefits. The agreement should be drafted by an attorney. Land trusts will normally have a deed that they commonly use that will reflect the land trust's "protection" concept, and can be tailored to the present owner's needs; however, owners are advised to seek the advice of an attorney of their choosing who will ensure that the conservation easement allows for the continued use of that land (i.e. for farming) by the grantor, with enough flexibility that will not otherwise endanger tax benefits. This deed will be recorded with the county register of deeds.

Note that many conservation easement deeds are drafted by the future holder of the easement, usually a land trust with a lawyer on staff or county with support from the county attorney. You should be aware that these attorneys do not technically represent your interests, and you should have your own attorney review the easement deed draft to ensure it does not needlessly impact your use and future transfer needs for the land.

2. *Inventory of the Property.* This document is known as the baseline report, and can be prepared by a biologist or other consultant familiar with the purposes of the intended conservation easement.This document supports any declaration of conservation purposes, and will also serve to illustrate the conditions of the property that the easement holder will not want significantly changed.

3. *Appraisal*. The appraisal is prepared by an independent appraiser, and should be hired by the landowner/grantor. The appraiser should be competent in conservation easement transactions. The appraiser will conduct essentially two appraisals: one for the land's highest and best use, the second for its value under the conservation easement restrictions. The difference represents the value of your donation or sale if you are to receive payment for the conservation easement.

4. Title work. There must be clear title on the property to determine true ownership and whether any encumbrances (such as deeds of trust or easements) exist. This work should be performed by an attorney.

5. *Survey and legal description*. As with any real estate transaction, there should be a survey and a legal description for the property, which can be provided by a surveyor.

6. *Form 8283*. This is an attachment to the federal tax return of all individuals claiming contributions more than $5,000, prepared by the Grantor or his accountant, and signed by the Grantor, Grantee and appraiser. If the deduction claimed is greater than $500,000, then the full appraisal must also be attached).

Note federal tax law requires the grantee organization to maintain sufficient assets to carry out its monitoring and enforcement obligations in the future. Therefore, organizations that agree to hold conservation agreements will have a stewardship fund or endowment set aside to pay for staff costs associated with monitoring. Therefore, they generally need to raise money to add to this fund whenever they add a conservation easement to their monitoring requirements. While it is not a requirement, the grantee organization will usually ask the grantor to contribute to the fund.

MODIFICATION AND REVOCATION Grantors of conservation easements should never make their decision based on the possibility that the conservation easement will be revoked or able to be modified. Conservation easements are designed to be permanent, so amendment can be difficult and extinguishment is almost impossible. In rare circumstances, extinguishment may be accomplished through a court proceeding. Successful extinguishment requires a convincing demonstration that, due to a change in circumstances (normally regarding the surrounding land use) use of the property for the original conservation purposes of the conservation easement are no longer practical or possible. If the conservation easement is extinguished, the interest in the land (or the proceeds from any sale) is allocated to Grantee and Grantor, respectively, in proportion to the value of the agreement and the value of the land. It is possible that a conservation easement can be amended by agreement of the owner and the holder of the easement. Such agreements can clarify an ambiguity in the easement, but cannot in any way diminish the conservation value upon which any tax deductions were calculated. Amendments also can add acreage to an easement or add further to the protection of the property. For instance, an increase in the conservation value of the easement, such as adding acres or relinquishing a parcel right that was

retained in the original easement could generate an additional gift value for tax purposes.

Remember that while a conservation easement can be a valuable tool, it is not a matter of right. Landowners must understand that holding and monitoring a conservation easement is a responsibility that a land trust or county must choose to undertake. Accepting an easement will depend on a number of factors, including a) the potential holder's organizational capacity, b) their conservation priorities, and c) the conservation qualities of your land or whether its use (in farming or forestry) aligns with the priorities of the organization.

For more information:

Washington State Office of Farmland Preservation
Washington State Conservation Commission http://ofp.scc.wa.gov/

Conservation Tools:
An Evaluation and Comparison of the Use of Certain Land Preservation Mechanisms
http://www.rco.wa.gov/documents/rco/ConservationTools.pdf

Washington Association of Land Trusts
http://www.walandtrusts.org

National or Regional Land Trust Alliance http://www.landtrustalliance.org

Notes

Section Four:

Meeting with Professional Advisers

Photo courtesy of Washington State University

About Lawyers and other Professional Advisers

Putting together a team of professionals to assist you is a necessary part of the farm transfer process. Though you and your family will accomplish a lot of work on your own, ultimately you will need professionals to advise you on financial matters and legal issues related to the future you want. You will need a lawyer to draft the documents to get you there. If you consider what is at stake - family harmony, protecting family wealth from unnecessary transfer costs, protecting the productivity of farm assets, continuing the flow of uninterrupted income to a farm enterprise – the time and money you spend on coordinating the process of farm transfer planning, including the time to carefully select and monitor your professional advisers and their fees, will have a very high rate of return.

Members of your team will include at least a lawyer and probably an accountant. At various times you could need the services of an appraiser, surveyor, insurance agent, and agents of financial institutions, including present and future creditors who must approve or finance certain transactions.

The time and money you spend on coordinating the process of farm transfer planning will have a very high rate of return.

The realities of putting together a competent "team" of professionals - one that effectively compliments each other's expertise and applies that expertise in a coordinated fashion to your particular circumstances – can be daunting. A primary challenge is determining who will coordinate the communication between professionals in a manner that you remain in the loop, and how to handle differences of opinion among your advisers on your particular situation and strategy.

Sometimes, a member of your family may volunteer for the task of coordinating the many assessments and information gathered as outlined in this workbook. This person may spend many hours reading up on subjects related to farm transfer planning, estate planning, arcane tax issues, as well as many hours on the phone with advisers, gathering information from family members, coordinating family meetings. There are other professionals that can serve in this purpose as well, either as a consultant, or as one of the members of your "team." Always remember that, unless you agreed otherwise, the relationship between you and your attorney is one of confidentiality, and much information and likely decisions will need to be kept from other family members.

Most farmers and rural landowners live in rural communities where personal relationships influence decisions. In such a community, one professional you customarily work with, perhaps a lender or insurance agent, refers you to other professionals and so on. In many cases, professionals will refer you to someone they have worked with before on other matters, and already have established mutual trust and lines of communication. Indeed, it makes little sense for one professional to refer you to someone in whom they have little confidence, as that will reflect directly on their professional credibility.

It cannot be avoided that the advice of some professionals will be tied to their offer of a certain product, such as insurance or financial investments, which are often necessary to meet your goals. There is nothing inherently wrong with this, and it is their compensation for offering you their critical expertise. Someone with the proper licensing – to protect you as a consumer – has to do it.

No one professional can provide every basic service. A lawyer cannot take a financial interest – other than compensation for his or her time – in your farm transfer transactions in the form of commissions from selling you an insurance policy or investments. Likewise, non-attorneys - such as financial planners, accountants, insurance agents - are likely breaking state law if they draft the legal documents you end up signing. If they offer to do it, you should decline, and you should refrain from requesting them to offer such advice, thinking it will save you money. You should be able to get a satisfactory explanation from each of your professionals on the necessity of each product, not simply that it is what someone else recommended or purchased. At the least, keep your lawyer and tax adviser informed of what financial products you contemplate purchasing.

About Lawyers
For a number of reasons, it is often practical to have the lawyer (also called attorney) serve as the central team member, often the point of first contact. One very practical reason: Attorneys ethically must accept responsibility for making sure clients fully understand what rights and opportunities they are giving up by choosing a particular course of action at the recommendation of a non-lawyer professional member of their team. Also, all communications are confidential.

Remember that the basic legal issues involved in farm transfer are not specific to you as a landowner or farmer, but generally apply to all members of society. Many transactions are routine. What differs is the landed nature of your wealth, your farm production interests that may govern your decisions, the unique aspects of farming as a small business owner and your role as caretaker of a land legacy. You should be confident your lawyer understands this.

Selecting a good lawyer can of course be a challenge. The lawyer most farmers and landowners come in contact with will be someone local in their community with whom they have done business before or who has served other members of the family. Often the issues surrounding farm transfer fall into a number of areas of legal practice – estate and gift tax planning, elder law, farm business operation (itself a host of practice areas) - and it is a challenge to find all of these in one practitioner. In some situations, families may consider having their local lawyer work with another lawyer on specialized issues on a limited and cost-effective basis.

A valuable lawyer, it must be recognized, is to effectively serve as a counselor to you and your family, not simply act as a plumber who fixes things that go wrong or executes documents at the direction of a non-attorney. You can help them and your family immensely by using the exercises in this workbook. The clearer your articulation of yours and your family's goals for the farm, the better service you will receive (i.e., you will feel as though you have been understood), and it will save you and your attorney time, which of course translates into money saved.

Lawyers are required to use independent judgment in considering how to serve your needs (ie. your goals), even when they have been referred to you by a non-attorney professional with whom you are doing business (e.g. a financial planner or insurance agent). Beware of any lawyer who simply complies with a recommendation on a course of action without thoroughly explaining it to you its significance. Your lawyer should be someone who makes you feel confident in their skills as a counselor, not just someone who prepares documents for you to sign.

Other professionals you will work with include:

Life insurance agents can review your insurance coverage and help you organize information for your attorney and tax adviser. The agent will suggest ways to help you avoid liquidity (cash flow) problems upon your death, and how to balance land and liquid assets. Be sure to request a proposal from any insurance professional recommending a certain product, and you should share any proposals for policies with your attorney to make sure the premiums and proceeds go in the right place. Price alone should not be the sole basis for purchasing life insurance as policies and the companies that underwrite them vary in strength.

Accountants or tax advisers are also knowledgeable of estate and other taxes. Certified Public Accountants are accountants who are licensed by a state board of accountancy. Accountants or other tax advisers (such as enrolled agents permitted to represent you before the Internal Revenue Service) will help you understand the tax consequences of various types of transfers, such as capital gains and depreciation recapture. Accountants or other tax advisers also can advise you about business or property management, valuation of assets, and business continuation or sale. Accountants or other tax advisers are usually compensated on an hourly basis.

Trust officers offer management and investment services. Trust officers may be attached to a bank trust department, or they may be independent. Trust officers are usually compensated based upon an annual percentage of the principal in the trust. In general, the larger the trust, the lower the percentage that you can expect to pay. Most trust officers have a minimum amount of money that they are willing to manage.

Financial planners review your entire financial situation and identify strategies to achieve your financial goals. They work with other professionals to develop your insurance, investment, retirement, and estate plan. Financial planners are compensated either on a fee basis or on a commission basis. The services of commission-based financial planners may be quite valuable to you, but the scope of their advice may be limited by the products that they sell. Fee-based financial planners generally do not sell any products.

Forestry professionals can advise you on an often overlooked asset: your forest stand. Many farms in Washington State have a forestry component which should be considered an asset and managed as such. It therefore should be critical to have a neutral, registered or certified forester. A forestry professional can help you a) develop a forest management plan, b) determine the volume and value of your timber, as well as its basis, c) conduct timber harvests and sales, properly reforest your land by advising you on how to best establish a new stand of trees, d) reduce your risk of loss from fire, insects, diseases, overstocked stands, and improve tax treatment of income, and e) enhance wildlife habitat and improve hunting success or increase wildlife viewing opportunities. Someone familiar with your timber stand, its age and value, can serve a valuable role in advising on property division and distribution in your estate plan.

Mediator

In a number of situations, you may find that communication is difficult within your family or those with interests in your farm property. A mediator is trained in consensus-building. Unlike the attorney, who ultimately represents one or more parties, a mediator is known as a "third-party neutral," one who is paid *not* to take sides. They can enforce the rules of communication, help explain positions, and keep the discussions on track. In a large family situation, this could prove very helpful.

Surveyors and Appraisers

Other professionals you will rely on will be surveyors and appraisers. In many cases, farm property will have been poorly described in previous deeds, and will need to be surveyed to determine the true boundaries for future recording (e.g. when transferring real estate to a limited liability company). Many land transfers will simply require a new survey, and sometimes you will want to separate contiguous property into separate tracts for distribution. Likewise, appraisers will be needed to value assets involved in the sale, gift or purchase of a business, real estate, or assets of a recently deceased parent for estate settlement purposes. The\ are also a requirement in many transactions, such as the sale or donation of a conservation easement.

Conclusion - Finding Services in One Store

For practical reasons as emphasized earlier, if you don't have a long-time adviser such as an accountant or insurance professional, your lawyer should be your primary coordinator of your legal and financial decision-making. In some cases, you may find that some of your essential services, particularly tax advice and perhaps accounting, can be housed within your lawyers firm. There are strict state rules in place to protect you in this arrangement. If there are sensitive matters that must be kept confidential the attorney-client privilege offers that protection.

Ultimately, you may have to travel outside your home county or region to find the right services, particularly legal and tax. Just as you might travel across the state to a farm show to shop for new equipment to enhance your farm income, doing the same to visit a lawyer will pay long-term dividends by protecting your wealth, the future of your farm, and the well-being of your family.

Gathering Information About Your Estate

Gathering as much information for working with your professional adviser(s) is extremely helpful. The clearer picture they have of your wealth, the type of assets you own personally or as part of your farm business, and where your land is located will give them a clearer picture up front of how to guide you. Otherwise, advice might be given and decisions will be made that could have been improved with better information. That said, it is understandable that there are limits to the time it takes to gather information, and the enormity of the task should not keep you from seeking out professional advice to guide you along sooner rather than later. As a practical matter, your farm transfer planning should be organized into a flexible framework, and by doing that your adviser will gain a clearer picture over time of the extent of your assets and your goals for distributing them.

Below are a number of information categories to help you start collecting and organizing the needed information a lawyer or tax adviser will likely want. The list covers many different types of assets, and may appear overwhelming. Just gather what you can but do not be too concerned that your adviser will not start working with you until it is complete. He or she will help you along with it as your relationship unfolds. There will be certain types of information that your lawyer will be able to uncover on his or her own, particularly real property and its relative value.

Like the worksheets on the following pages, many attorneys, tax advisers, and financial advisers have their own forms that they will ask you to use when compiling this information prior to your initial meeting. Organizing and gathering information by the following categories can greatly facilitate that process.

Personal Information
List the full names of your family members (ie. your children) and any other individuals with whom you own property. Be sure to include all oI your children, including those adopted and those already born to your current spouse before you were married (i.e. your step-children). List the names of your grandchildren, and which child of yours they belong to. List the names of other individuals with whom you co-own a business, and the names of your landlords and/or your tenants. This will be helpful to your lawyer to conduct what is known as a “conflict of interest” check, to make sure that he or she is not stumbling into a situation whereby they cannot serve you. If you are divorced, it is helpful to have copies of any divorce settlements or decrees and any premarital agreements from your current or earlier marriages.

Your personal information should include information about special needs children who may need help when they become adults. Also include information about parents or siblings who may need special provisions in your estate plan due to degenerative diseases or other conditions.

Bank Accounts
Provide as much information as possible for all bank and credit union accounts. Try and include the exact name(s) on each account and the name and location of the branch at which you do business. If any of your accounts are survivorship accounts, you should also provide the name of the beneficiary(ies) for that account. For joint accounts, please identify the joint owner.

Stocks, Mutual Funds and Bonds
Include a general description of all stocks, mutual funds and bonds, as well as their location. If you work with a financial planner, provide his or her contact information to your lawyer. You should give your financial planner a heads up that your lawyer might be calling with questions.

Life Insurance
List the types and amounts of life insurance you own, as well as the beneficiary and the benefit amount. If you have the policies, bring them to your lawyer so he or she can understand your insurance situation. If you have summary statements from your insurance agent or broker, bring those, or otherwise call them and find out what authorization they need from you to provide in-force illustrations of your current insurance holdings directly to your lawyer upon request.

Trusts
If you are a trustee of a trust established by someone else, let your lawyer know. If you have established

any trusts already as a part of earlier estate planning by another lawyer, please bring a copy of the trust to your meeting. If you are the beneficiary of any trusts, let your lawyer know and if at all possible bring a copy of that trust.

Personal or Business Loans Owed to You Describe any moneys owed to you. Include the debt amount, what it was for, how much is outstanding, the year you made the loan(s), and of course the person(s) indebted to you. Try to include copies of documents that provide evidence of or secure the debt.

Real Estate
If you have maps, aerial photographs, FSA farm numbers, etc. of your land, bring it to your meeting with your lawyer. As a practical matter in this modern digital age, simply providing your lawyer with the names of the counties where you own land will be enough for your lawyer to find out how much land you own, and a snapshot of how much it is worth (at least according to the county tax assessor). If you have deeds and such, bring them. If your county does not have this information online, your lawyer will help provide you a framework by which you can inform him or her more information on your land holdings. If you are not currently farming your land, give the names of any tenants who are.

Personal Property
List numbers of livestock, farm machinery, crop inventory, and any unique or valuable items of home furnishings, jewelry, art, antiques, and personal items. For unique personal items and family heirlooms, try and describe each item's cost and value, and include the names of any co-owners or who you inherited the property from. For farm assets, bring at least a depreciation schedule for the previous year. If you have been storing gold for many years, please let your lawyer know (this is not as uncommon as it sounds).

Personal and Business Debts
Compile a list of all money that you owe to others. This list should include information for each creditor, the amount and terms of the debt, and the security, if any, for the loan. For farm equipment that still has a lien, simply identify it and the remaining balance on the depreciation schedule you provide (see above). For debt secured by your real property, let your lawyer know who you do banking with and your contact there (like with the other advisers, be ready to let your lender know the lawyer will be calling with questions) If you have other debt attached to your real property, such as tax liens, judgment debt or workmen's liens, include all information to the extent known. Information about all other personal liabilities.

Retirement Benefits
If you have significant pensions or retirement benefits, make these known to your lawyer. Try to list and describe all pensions, profit sharing, deferred compensation, death benefits and social security benefits, their source and amounts paid and when. Be sure to include names of any beneficiaries other than yourself.

Other Financial Information
Be prepared to provide a picture of your income situation from farming operations and land rent.Bring copies of income tax returns for at least the last two years to the first meeting with a lawyer.

Safe Keeping; Safety Deposit Boxes, Safes and Fireproof File Cabinets
If you have a safe deposit box, please let your lawyer know its location and contents. Describe the locations where you keep your important papers (there is a worksheet on the following page to help with this task).

Worksheet 4.1

Locate Important Documents

Use this worksheet to help locate the documents you will make your lawyer's job easier. It is important to gather certain documents to assess your current financial situation, but also to determine ownership and obligations related to your real and personal property. Doing this exercise prior to meeting with professionals will save time, money, and will help them better serve your needs. Sample answers can include "file in home office", "safe deposit box at [bank]", "lawyer's office", "home computer", etc.

DOCUMENT	WHERE IS IT?
Birth Certificates (all family members)	
Marriage Certificates	
Divorce decrees/separation	
Medical Records	
Healthcare Power of Attorney and Living Will	
Durable Power of Attorney	
Bequest list of tangible personal property	
Wills and Trust documents	
Cemetery deeds/burial instructions	
List of special bequests (to heirs, charity, etc.)	
Insurance policies	
Stocks, mutual fund and bond certificates	
Real estate deeds (county registries)	
Promissory notes, contracts, mortgages, receivables	
Partnership/corporation documents	
Checking/savings account statements	
Pension statements	
Income/gift tax returns	
Farm and other business financial statements	
Farm conservation contracts (NRCS, etc.)	
Forestry Management Plan	

Worksheet 4.2

Will and Trust Basic Decisions

Regardless of the size of your estate, all wills and trusts require basic decisions about who will administer the estate or trust property, whom property will go to, how it will be divided, etc. Use this worksheet to help make some decisions on key elements of your will and trust documents. Factors to consider are noted with each question.

PERSONAL REPRESENTATIVE(S) (aka EXECUTOR(S)): Probate is the process of administering one's affairs at death through a court process. When a person dies with or even without a Will, a probate is most often required to get things in order so assets can be distributed. While there are ways to bypass probate, if parts of your estate pass through probate, you need to select who you believe can handle the details of paying your debts, filing probate documents, paying possible estate taxes, and distributing the remaining assets to the beneficiaries named in your will. This person is referred to as the Personal Representative in Washington, or the Executor or Executrix. A spouse is appropriate as well as adult children, close friend, accountant, lawyer (subject to ethical disclosures), or a bank's trust department. The individual is generally paid. Successors (1 or more) should be named in case the first predeceases you or is incapacitated or is otherwise unable or unwilling to serve.

Name/Address: ____

Successor(s): ____

TRUSTEE(S): If you are advised to make use of a trust, whether in your will or in a separate revocable or irrevocable trust, you will need to name a trustee to manage investments, pay taxes, make decisions about income and principle distributions, and so forth. In the event he or she cannot serve, you will want to provide for one or more successor trustees. Normally if you form a revocable trust (one you can change) you will be its first trustee, with your spouse taking over following your disability or death, then a trusted family member or institution taking over upon death or incapacity.

Name/Address: ____

Successor(s): ____

You may be advised to select a corporate or individual fiduciary as executor or trustee, depending on your family situation. Trustees (just like Personal Representatives for an estate) are referred to as fiduciaries because of the high standard of care required of them to manage the assets of another person.

GUARDIAN(S) (for minor children): For parents with minor children using this workbook, it is important to accept the possibility that you could, through accident or illness, predecease your children. It is strongly advisable to nominate a guardian for your children in the body of your will, and also in your durable power of attorney should you become legally incapacitated as permitted in Washington State A thorough discussion of who might best serve as the guardian of your children in that event should take place before drafting or updating your wills. It is important to identify secondary and third guardians in the event your first choices are unable through changed circumstances to serve or otherwise care for your children. This will provide clarity of your wishes to your family and friends.

Factors to consider would include: age of proposed guardians and ages of their children; ages of your children and the number of them who are still minors; and health and financial situations of all parties. If you name a couple as guardians and one of them dies, would you want the surviving co-guardian to act as sole guardian? What if they divorce? Is a brother, sister, grandparent or a close friend the better choice? Be sure to discuss the matter with your intended choices to make sure they are willing — or otherwise feel confident they are able —

to serve as guardians for your children. Remember that your will is merely a suggestion to the court, but in all likelihood the suggestion of guardian will ensure your children are cared for according to your wishes.

Name/Address: ____

Successor(s): ____

DISTRIBUTION OF ASSETS TO SPOUSE: Much of your property will be jointly owned and may pass immediately to your spouse; if you have a written community property agreement with vesting language in it, all community property can do so as well. For assets you own individually, i.e. "separate" property as defined under Washington law, you will need to decide whether to pass those to your spouse or someone else. Should assets be held in trust for management purposes, estate tax management or incapacity of spouse? Your attorney may advise the use of a revocable trust to protect your estate tax exemption while providing care for your spouse for her lifetime. Keep in mind that unlike in Washington, in many states your spouse is entitled to a certain share of your estate (unless he/she has executed an enforceable prenuptial agreement), and a devise smaller than the statutory level may add expense to the estate in determining a statutory share. There is a provision in Washington for a spousal claim, but it is a limited one and generally granted for need.

DISTRIBUTION OF ASSETS TO CHILDREN: If you do not want your assets distributed outright to your children in the event of your demise, assets should probably be held in a trust. A "testamentary trust" can be created in your will as contingency provisions for underage children, particularly if your estate is still relatively modest. Alternatively, you can use a revocable trust with contingency provisions. The trustee will take care of minor children's needs as instructed in the trust. At some future time you will probably want to distribute the assets to the children. At what age? What about a child with disabilities? What about grandchildren?

Many people like to distribute a portion of the estate at several different times during their children's lives. (For instance, distribute at age 21, at age 25, and at age 30; or ½ at age 30 and ½ at age 35, etc.)

Your preference: ____ % at age ____ ; % ____ at age ____; % ____ at age ____.

Other Key Considerations:
1. Do you want the estate to pass in equal shares to children?
2. Do you want some to have more because others have had more in the past or to provide adequate opportunities to keep the business in the family?
3 Do any of your children have special needs? If so, your lawyer should advise you on trusts designed to benefit your children while allowing them to maximize available support payments (ie. Special or Supplemental Needs Trusts)

DISPOSITION OF REMAINS: If you have a specific idea of whether you want to be cremated or where you want to be buried, your will is the proper place to make it known.

CHARITABLE BEQUESTS: You can specify charitable bequests in your will and/or trust. These can include your church, your school alma mater, or a non-profit organization whose mission you support. For very large gifts you should have your attorney pre-plan with the recipient institution, particularly where the gift is land.

INDIVIDUAL BEQUESTS: Often there are special heirlooms or gifts of family treasures that you want specific individuals to have. (Attach sheets as necessary) You have the ability both in your will and trust to distribute specific items, this may help avoid confusion between heirs interested in the same item without knowing your preference. Many trusts incorporate "personal property memoranda" whereby you can efficiently instruct your future Trustee on distribution of certain assets. Use additional sheets if necessary.

Worksheet 4.3

Gathering information about your estate

Use this worksheet to take stock of your personal wealth, your family situation, and your current plans and ideas, so that your professional advisors will have a good starting point from which to guide you through the farm transfer planning process.

I. PERSONAL INFORMATION Date: ____________________

Your Full Name: ____

Birth Date: ____________________

Spouse's Full Name: ____

Birth Date: ____________________

Date, County, and State of your marriage: ____

Home address: ____

Home telephone: ____________________ Email address: ____________________

Business Name(s) and Address(es):

Husband: ____

Wife: ____

Business telephone: Husband ____________________ Wife ____________________

II. PROFESSIONAL ADVISERS:

Attorney: ____

Address: ____

Telephone: ____ Email address:

Insurance Agent:

Address: ____

Telephone: ____________________ Email address: ____________________

Financial Adviser:

Address: ____

Telephone: ______________________________ Email address:

Accountant: ____

Address: ____

Telephone: ______________________________ Email address:

Lender: ____

Address: ____

Telephone: ______________________________ Email address:

Other Advisers: ____

____

III. ALL CHILDREN: (if any children are adopted or from a previous marriage, please indicate)

Name	Spouse	Date of Birth	Resides (City, State)

III.B. GRANDCHILDREN:

Name	Parent	Date of Birth	Resides (City, State)

IV. GENERAL FAMILY INFORMATION:

Does any child or grandchild have a health problem or handicap? Yes No

If yes, please explain: ____

Are there any persons dependent on you? Yes No

Monthly obligation: Alimony or child support $ and years to be paid: ______________________________

V. CURRENT ESTATE PLANS:

Does Husband have a will/trust at the present time? Yes No

Location of original(s): ____

Does Wife have a will/trust at the present time? Yes No

Location of original(s): ____

Do you have a marital property agreement? Yes No

VI. REAL ESTATE (Personal residences, farm properties, rental properties)

Location	Ownership*	Basis**	Estimated Value	Mortgage Balance

VI.1 TIMBER REAL ESTATE (Timberland, merchantable timber, pre-merchantable timber)

Location	Ownership*	Basis**	Estimated Value	Mortgage Balance

*List the name(s) that appear as grantees on the deed for each property to the best of your knowledge. If you are certain the deed contains language such as “jointly” or “with right of survivorship,” please indicate. Alternatively, provide the counties where you own land, your lawyer can likely find all properties online.

**Basis is the value of the property at the point you came into its ownership, less any depreciation taken, and is determined by the manner in which you acquired it. As a general matter, if you inherited it, your basis is the value placed on it during the estate settlement. If you purchased it, the purchase price is your basis. If the property was gifted to you, generally your basis is the same as the previous owner’s. Basis is used to determine any capital gains you or your heirs may be exposed to by sale of the property.

VII. BANK ACCOUNTS AND CERTIFICATES OF DEPOSIT:

Institution Name	Type of Account	Ownership	Approximate Balance

VIII. STOCKS AND MUTUAL FUNDS:

Company/Fund	Number of Shares	Ownership	Cost (Basis)	Market Value

IX. BONDS (Taxable and Exempt), TREASURY INSTRUMENTS, NOTES RECEIVABLE:

Description	Due Date	Face Value	Market Value	Ownership

X. LIFE INSURANCE

Furnish the requested information for all policies on members of your family, including husband, wife and children. Be sure to include group insurance a member of your family may have through an off-farm job. Use additional sheets if necessary. Your insurance agent may be able to provide you with printouts of the information requested below.

	Policy 1	Policy 2	Policy 3
Insurance Co.			
Policy #			
Insured			
Owner			
Type Insurance			
Face Value			
Cash Surrender Value			
Loans			

Primary Beneficiary			
Contingent Beneficiary			

XI. RETIREMENT PLANS

If either spouse is entitled to any benefits under a deferred compensation, retirement or profit sharing plan, please provide the following information.

	Plan 1	Plan 2	Plan 3
Participant			
Plan Name			
Plan Nature			
Expected Payment			
Death Benefit			
Contributions...			
...Made by			
Designated Beneficiary			
Life Insurance in Plan?			

If either spouse has established an IRA account, please furnish the following information:

Contributor			
Investment			
Approximate Value			
Designated Beneficiary			

XII. INTEREST IN TRUSTS OR ESTATES:

Does any member of your family have any relationship to an existing trust as donor, trustee or beneficiary? Yes No

Has any member of your family in the past received an inheritance from an estate? Yes No

If yes, please explain:

Does any member of your family have any interest (e.g. as a beneficiary) in a pending estate? Yes No

If yes, please explain:

XIII. PERSONAL EFFECTS:

Please list all items having significant market value, such as jewelry, art, antiques, rare musical instruments, autos, boats, collections, farm equipment, etc. Please Note: Normal household furnishings need not be listed.

Description	Ownership	Estimated Value

XIV. CLOSELY HELD BUSINESS INTERESTS:

Company Name	Organization Type (Corp., LLC)	Ownership Interest (as a %)	Estimated Value

XV. LIABILITIES (other than real estate mortgage):

Creditor	Amount Due	Date Payable	Collateral Description

XVI. GIFTING:

Have you or your spouse made any gifts in any one year since 2010 to any person which exceeded in value either a) $13,000 if made by you alone, or b) $26,000 if made by you and your spouse? Yes No

If yes, specify the amount of gift, date and donee:

Gift Description	Estimated Value	Date of Gift	Donee

Notes

Glossary

1031 Exchange: Also known as a "Like-Kind Exchange." A structured exchange, enabled by the Federal Internal Revenue Code, whereby taxes on capital gains realized from the sale of property can be deferred when sale proceeds are used to purchase property of like kind.

Accountant: One who is skilled in the practice of accounting; a professional with skills in accounting, auditing, financial management and/or tax law.

Acre: A measure of land equaling 160 square rods, or 4840 square yards, or 43,560 square feet.

Administrator: A person appointed by the court to manage and settle the estate of a deceased person who died intestate (without a will). Washington generally calls all persons administering an estate a personal representative.

Ad valorem: Literally, "according to value", the designation of an assessment of taxes against property.

Agricultural Conservation Easement: Generally describes a voluntary agreement which restricts land to agricultural uses.

Agriculture: The science, art, or practice of cultivating the soil, producing crops, and raising livestock and in varying degrees the preparation and marketing of the resulting products; farming; the use of land for growing crops, livestock or timber.

Alimony: An allowance to a spouse for support given by another spouse due to a separation or divorce.

Annexation: The process by which land outside of any incorporated municipality is taken into the legal boundaries of a municipality.

Appraisal: An estimate or opinion of quantity, quality, or value. A documented opinion as to a property's value, marketability, usefulness, or suitability for a purpose.

Appreciation: The increase in the value of property due to economic or related causes that may be temporary or permanent.

Appurtenance: A feature of a parcel of land, such as a right, privilege, improvement or fixture that passes with the land. For example, an easement is an appurtenance.

Arbitration: A process intended to settle disputed questions or law or fact, by one or more arbitrators by whose decisions the parties agree to be bound. An "arbitration clause" can be found in contracts between parties.

Assessment: A charge against real estate made by a unit of government to cover the proportionate cost of an improvement, such as a water line or sewer.

Assignment: the transfer of one's rights under a contract to another person.

Assignment of Lease: A transfer by a lessee (tenant) of all interest under a lease for the balance of the term of the lease. May be restricted by the terms of a lease.

Attorney: A person licensed to practice law in a particular state.

Attorney in Fact: one who is authorized to perform certain legal acts for another under a power of attorney. See *Power of Attorney*.

Bargain Sale: The sale of property to a charitable organization for less than its fair market value. This approach gives the landowner the opportunity to exchange the value not received in cash for a reduction in state and federal income taxes.

Basis: the price paid for property or the fair market value of property when inherited, less accumulated depreciation, used to calculate capital gains on income from the sale of the property.

Beneficiary: One for whose benefit a trust is created, for whose benefit property or funds are placed in trust or the recipient of funds from an insurance fund or annuity contract.

Boiler plate: Language considered standard to contracts and other written agreements. Paragraphs of boiler-plate can appear identical in any number of contracts.

Bundle of Legal Rights concept: Establishes real estate ownership; consists of rights to sell, to mortgage, to lease, to will, to regain possession at end of a lease (reversion); to build and remove improvements, to control use within the law. Such legal rights in land can be transferred in all or in part.

Capital: Accumulated wealth used for production of additional wealth.

Capitalization: A process used by appraisers to convert a property's actual or projected net income into an estimate of property's value.

Capital Gain: Profit that results from the sale or exchange of an asset.

Caveat Emptor: "Let the buyer beware," legal term to describe the duty of a buyer of property to examine the property, and the property purchase is subject to conditions which would be readily ascertainable upon inspection.

Chain: A surveyor term for a distance measuring sixty-six (66) feet. Commonly seen in property descriptions in older deeds.

Chain of Title: A history of conveyances and encumbrances affecting the title to particular real property, found in the deed registry of the county where the property is located.

Charitable Deduction: The value of a donation to a nonprofit organization, or public agency that can be used to decrease the amount of taxes that are due from an individual. An easement or land donation must be permanent to qualify as a charitable deduction.

Charitable Gift Annuity: A method of donating assets, including land, directly to a qualified conservation organization which is then responsible for making annual payments to the donor for a specified period of time. In one variant to this option, donors can defer their annuity payments to a later date, such as at the time of retirement.

Charitable Remainder Trust: A method of donating land to a third-party trust (managed by a bank or financial institution). The trust is responsible for handling the donor's annual payments and, upon his/her death, transfers the remaining assets to the designated conservation group.

Codicil: A written supplement or amendment to an existing will.

Community Property: Property acquired during marriage is presumed to be owned by the marital community, with each spouse owning an undivided 1/2 of the whole. Community property is a matter of law in Washington. Facts can be used to demonstrate that property is separate property of either husband or wife, and arises from ownership prior to marriage, received by gift or by inheritance. Comingling can destroy separate property and converts it to community property. Either spouse can manage community property. A spouse can bequeath his or her share to any person… but community property would go to a surviving spouse by law if no other plan was in place, albeit through probate.

Community Property Agreement: A written agreement creating or confirming that specific property is community or separate property. It may be used to avoid a probate if it contains vesting language conveying community property to a surviving spouse. Such a provision may not be advisable in the event that estate tax avoidance planning using trusts is recommended.

Contingent beneficiary: The person to whom the proceeds of a life insurance policy are payable in the event that the primary beneficiary dies before the insured.

Corporation: A complex business entity owned by shareholders who bear no liability for business debts beyond the price paid for their shares of ownership.

Conservation Easement: A restriction on particular uses of land in order to advance specific goals to protect or preserve a parcel of land.

Conservation Tax Credit: A credit against state income tax owed, available to individuals and business entities, for the donation of real property, or a perpetual conservation easement, to a qualified entity.

Conservation Values: The aspects of a tract of land, such as scenic views, cultural resources, historic structures, wildlife habitat, water features and water quality benefits, agricultural use, rare plant species, wetlands and similar features worthy of long-term conservation and/or preservation.

Contract: A legally enforceable agreement between two or more competent parties supported by legal consideration to do or refrain from doing some act. Contracts for real property or for value above a certain amount must be in writing.

Covenant: A deed or land restriction that is intended to limit the use of the land by the current owner and all future owners. It is a non-possessory interest in land, such as an agreement between adjoining landowners to do something (affirmative covenant) or to refrain from doing something (restrictive covenant) with respect to the land. Each covenant has two sides: the burden and the benefit. The burden is the promisor's duty to perform the promise and the benefit is the promisee's right to enforce the promise. Some covenants may not be perpetual.

Decedent: A deceased person.

Deed: A signed writing under which an interest in real property is transferred from a grantor to a grantee upon delivery of the writing to the grantee.

Deed Restriction: A limitation in a deed to a parcel of property that seeks to limit the use of that parcel by the subsequent owner. Some deed restrictions may not be perpetual.

Deed of Trust: A recorded deed, held in place of a mortgage, to indicate in a chain of title that there is a lien on a property. A trustee holds legal title until the lien is paid.

Development Rights: The term applied to a landowners right, subject to governmental restrictions such as zoning, to develop property for non-residential uses.

Devise: A gift of real property by the will of a decedent.

Devisee: A person to whom lands or other real property are given by a will.

Dominant Tenement: A parcel of land that carries a right to use all or a portion of a neighboring parcel of land, such as an easement providing access across another's land.

Durable Power of Attorney: The durable power of attorney is identical to the regular power of attorney except for one crucial difference. The regular power of attorney ceases to be effective if you become disabled, whereas the durable power of attorney continues to be effective despite your subsequent disability.

Easement: An implied or express agreement (written or oral) creating a right, privilege or interest by one party in another party's parcel of land.

Eminent Domain: The right of a sovereign state to take private property for public use.

Equity: The interest or value an owner has in an asset over and above the debts against that asset.

Escheat: The reverting of property to the state when there are no persons legally entitled to hold title or when there are no heirs to inherit property.

Estate Tax: A federal tax on the value of all assets owned at the time of death. This tax is paid out of the estate of the deceased, before assets are transferred to the heirs (normally within nine months of date of death). The amount of the tax is based upon the total value of the estate less any applicable deductions.

Executor: A man chosen by the maker of a will to carry out the terms of the will.

Executrix: A woman chosen by the maker of a will to carry out the terms of the will.

Extra Territorial Jurisdiction (ETJ): The legal ability of a municipality to exercise authority beyond its normal boundaries.

Fair Market Value: The price that a willing buyer would pay a willing seller at a time when neither party is under any compulsion to buy or sell and both being fully informed of the relevant facts.

Farmland Protection Program: A program that uses public monies or public authority to prevent the development of farmland for non-agricultural purposes.

Fee Simple: The largest estate or ownership in real property, free from all manner of conditions or encumbrances.

Fiduciary: A relationship based upon trust or confidence. A person having a duty to act in the best interest of another.

Fixture: An item of personal property affixed to a building or structure on land in such a manner that it becomes a part of the building, structure or real estate. Fixtures affixed to real estate become appurtenances of that real estate, and thus pass with the transfer of that real estate. See *Appurtenances*.

Grantee: Term used to describe the person or entity that receives a transfer of an interest in property by sale, gift or trade.

Grantor: Term used to describe the person or entity that relinquishes an interest in property by sale, gift or trade. For example, a grantor conveys land to a grantee by deed.

Ground Lease: The separation of ownership of land from ownership of buildings and improvements to the land. The lessee under a ground lease pays rent to the landowner but owns the improvements outright.

Guardian: A person appointed by a court who has custody and care of a minor child or incompetent adult. A guardian can be named in a will.

Healthcare Power of Attorney: A written grant of authority from one individual to another to make decisions regarding significant health care decisions in the event the first individual is unable to express their wishes for care.

Heir: A person appointed by statute to succeed to the estate of a deceased person in the case of intestacy.

Heir Property: Land that is owned as tenants in common by two or more people who have inherited the land through intestacy. Heir property may have owners with varying fractional interests from several generations.

Highest and Best Use: That realistic potential use of property which will, as of the date of an appraisal, support the highest market value for the property, or that use which will produce the maximum net return on the property over the period encompassing the foreseeable useful life of the property.

HIPAA Waiver: A document nominating HIPAA (Health Insurance Portability and Accountability Act of 1996) personal representatives having access to protected medical information and status of an individual. HIPAA is the federal privacy statute safeguarding certain medical information, and Washington has similar protections in place.

Impact Fees: Fees required of a developer for land disturbing activities that are assessed by a governmental unit based upon a formula.

Improvements to land: Any betterment to land that increases its value or use.

Income Tax Credit: A decrease in state income tax due in exchange for a permanent donation of an easement or land to a qualified land protection agency or nongovernmental organization.

Income Tax Deduction: A decrease in taxable income.

Inherit: To succeed in ownership of property by devise or law at the death of the property's owner.

Inheritance Tax: A tax paid by estate beneficiaries to the state and federal government. The percentage of tax paid is determined by the size of the inheritance, as well as the beneficiary's relationship to the deceased.

Installment Contract: Purchase of property by two or more payments over time.

Inter vivos Trust: A trust created while the creator (called a trustor or settlor) is alive, sometimes called a "living trust." The property is placed in trust with a trustee (often the trustor during his/her lifetime) and distribution will take place according to the terms of the trust — during the trustor's lifetime and/or upon the trustor's death.

Intestate: To die without a valid will. Property of the decedent is passed to heirs at law according to a statutory scheme.

Irrevocable Inter vivos Trust: A permanent trust created during a grantor's lifetime. Once it is created, it cannot be revoked, amended, or changed in any way.

Joint Tenancy: Property held by two or more persons together whereby the death of one owner transfers that interest to the other owner(s).

Land Contract: A contract for the purchase of real estate upon an installment basis, whereby the seller retains title until the last installment payment is made by the purchaser.

Landowner: An owner of land and its appurtenances.

Lawyer: A person licensed to practice law in a particular state.

Lease: A contract, written or oral, for the possession of property in return for payment of consideration, such as money (i.e. rent).

Lease-Option Agreement: An agreement to lease property that also extends to the lessee, an option to purchase the leasehold interest at a future date.

Lease-Purchase Agreement: An agreement to lease property that also binds the parties to complete a purchase and sale of the property at a future date.

Leasehold: The interest a lessee has in real estate by virtue of a lease.

Legacy: A disposition of personal property under a will.

Legatee: A person who receives personal property under a will.

Lessee: The person who leases property from the owner of the property.

Lessor: The person who owns property and leases it to a non-owner for use.

Legal Description: A description recognized by law which is sufficient to locate and identify real property.

Letter of Last Instruction: A letter of last instruction leaves basic information to survivors upon your death. Rather than forcing survivors to become detectives and find all of your important papers, you can provide the details and instructions in one document. Always attach a copy of the instructions to your will.

Liability: In law, an obligation of one party to another, usually to compensate financially. It is an aspect of tort law that results from damage, injury, or a wrongful act.

Life Estate: An estate or interest held during the term of some certain person's life. With the creation of a life estate, there are two types of beneficiaries: a life tenant and a remainderman. When granting a life estate in a property you will also need to identify one or more remaindermen; those who will come into possession of the property at the life tenant's death by operation law.

Life Insurance Trust: A trust funded by life insurance. The grantor names the trust fund as the beneficiary of the life insurance policy. When the insured dies, the trust is funded by proceeds from the insurance.

Life Tenant: One type of beneficiary in the creation of a life estate. The life tenant has the right to use and possess the property for the life of a tenant or another person.

Limited Liability Company (LLC): A form of business entity often referred to as a "hybrid" of the corporation and partnership forms of business entity. Owners are generally referred to as members. An LLC is governed by an written *Operating Agreement*.

Limited Partnership: A partnership in which at least one partner has his or her liability limited to the loss of the capital contribution that he has made to the partnership. A limited partnership requires the execution of a written partnership agreement.

Living Trust: See *inter vivos* trust.

Living Will: A notarized and witnessed document that expresses the creator's wishes that he or she not be subject to extraordinary medical procedures that prolong the dying process.

Marital Property Agreement: State laws empower and restrict the actions of married persons. Real and personal property of any married person that is acquired before the marriage, or which he or she may become entitled to after marriage, remain the sole and separate property of that married person. A marital property agreement clarifies the rights and obligations of each spouse with respect to such property.

Market Value: The highest price which a willing buyer would pay, and the lowest a willing seller would accept.

Mediation: A process whereby a third party assists two contending parties in voluntarily settling their dispute(s).

Metes and Bounds: A description in a deed of the location of a parcel of land where the boundaries are defined by directions and distances.

Mineral Deed: A deed transferring mineral rights, severed from surface rights, to a grantee.

Mineral Lease: A lease entitling the lessee to explore for minerals and mine them if discovered.

Nonconforming Use: A use of land that predates zoning, and is not in accordance with the uses prescribed for the area by a zoning ordinance. Such a use may be continued, but generally not expanded.

Nongovernmental Organization (NGO): A charitable organization that is committed to one or more causes that address and improve the world around us.

Nonprofit: An organization that operates for the purpose of assisting other individuals, groups, or causes rather than garnering profits for themselves.

Nuncupative Will: An oral will declared and dictated by a testator in his or her last illness in front of witnesses and thereafter reduced to writing.

Open Space: Public and private undeveloped land such as a park, farm and forest land

Option: The right to purchase or lease a property at a certain price for a certain designated period of time, for which right consideration is paid.

Partition: A division made of real property among those who own it. Can be voluntary or court ordered by a special proceeding.

Partnership: A voluntary contract between two or more persons combine money, labor, and/or skill for the purpose of making a profit, with the understanding of a proportional sharing of profits and losses between or among them. Partnerships can be created under written contract or implied by law due to actions of the parties.

Partnership Agreement: A document which embodies the terms and conditions of a partnership.

Percentage Lease: A lease of commercial business property in which the rental is based upon the volume of sales made upon the leased premises.

Permanent or Perpetual Conservation Easement: A conservation easement that is written so that it does not expire. Only a permanent easement qualifies a landowner for tax breaks.

Personality: Personal property (ie. not real estate)

Pour Over Will: The will of a person who has already executed a trust wherein all property is designated to be distributed or managed upon the death of the person whose possessions are in trust, leaving all property to the trust. A pour over will assures that any assets that somehow were not included in the trust become assets of the trust upon the party's death.

Power of Attorney: A written instrument authorizing a person to act as the agent or attorney in fact of the person granting it; such power may be limited or general according to the terms of the instrument, and need not be given to a lawyer.

Premarital Agreement: An agreement between prospective spouses made prior to a planned marriage. The agreement becomes effective upon marriage. Agreements between people living together but not contemplating marriage, and post-nuptial or separation agreements are not included in this law. A premarital agreement must be in writing and signed by both parties -oral agreements cannot constitute premarital agreements.

Present Use Value: The term used to describe the

Tax Credit: A dollar-for-dollar reduction in the income tax payment required of a person.

Tenancy at Will: A license to use or occupy lands at the will of the owner that can be cancelled at any time.

Tenancy for Years: The leasing of property for any fixed, definite period of time, whether such period be one week, one month, one year, ten years, or any other definite period of time.

Tenancy in Common: A form of property ownership held by two or more persons, each of whom is considered to have rights in the entire property.

Tenant: A person who holds real estate under a lease.

Testamentary Trust: A trust created by a person's will, thereby not effective until the death of the testator. Testamentary trusts are used chiefly by individuals who are concerned about their beneficiaries' ability to administer large amounts of assets.

Testate: Leaving a valid will at death.

Testator: A person who makes a will is called a testator (male) or testatrix (female).

Tort Liability: A "tort" is an injury to another person or to property, which is compensable under the law. Categories of torts include negligence, gross negligence, and intentional wrongdoing. Negligence is the most common type of tort. To give rise to a legal claim in negligence, an act (or inaction) must satisfy four elements:

1. there must be a legal duty of care to another person;
2. there must be a breach of that duty;
3. the claimant must have suffered damages, and
4. the damages must have been proximately caused by the breach of duty.

Trust: A legal arrangement, evidenced by a written instrument, whereby a grantor transfers the legal title of property to a trustee to hold and manage that property for the benefit of a third person (a beneficiary).

Trustee: An individual or corporation named by an individual, who sets aside property to be used for the benefit of another person, to manage the property as provided by the terms of the document that created the trust.

Undivided Ownership: Ownership of a fractional interest in property by sharing possession of the whole (undivided) property with one or more co-owners (co-tenants).

Will: A written document which, when properly executed (signed and witnessed) is effective at the death of the maker to dispose of property according to the terms of the document.

Working Lands: Term of art describing farm, forest and horticultural land that is kept in it's intended use for the purpose of generating income.

Zoning: The exercise of police power of a municipality or county in regulating and controlling the character and use of property. Zoning commonly includes regulation on the kinds of activities which will be acceptable on particular lots (such as residential, agricultural, commercial or industrial) and the densities at which those activities can be performed.

Notes