

# Transferring the Farm: A Survey of Legal Considerations



**LAND FOR GOOD WORKSHOP**

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# Disclaimer



- This presentation is not legal advice and no attorney-client relationship exists.
- The materials presented are for informational purposes only.
- Farm transfers are highly specific to the particular needs of a farm operation. You should contact your attorney before implementing any particular transfer strategy.

# Transferring the Farm



# Overview



- **General Considerations**
- **Business Tools**
- **Property Tools**
- **Estate Planning Tools**
- **Transactional Tools**

# What is involved in a farm transfer?



- **Transfer of ownership**
- **Transfer of control**
- **Transfer of revenue/risk**

# Business Tools



- **Sole Proprietorship**
- **Partnership**
- **Limited Liability Company (LLCs)**
- **Corporations**

# Factors to Consider



- **Tax Liability**
- **Liability (debts/actions)**
- **Ease of Transfer**
- **Management**
- **Raising Capital/Allocating revenue**

# Sole Proprietorship



- **Advantages**

- Simple (tax and otherwise)
- Inexpensive to operate

- **Disadvantages**

- No liability protection (for assets/actions)
- Personal assets not shielded from farm debts
- Farm transfer/investment can be cumbersome
- Business dies when you do



# Partnership



- **Advantages**

- Pass through taxation (each partner recognizes/reports gains/losses)
- Simple to operate (either implied or formal)
- Inexpensive to operate
- Provides a mechanism for decision-making

- **Disadvantages**

- No liability protection (for assets/actions)
- Liability for partner's acts (individually and jointly)
- Transfer to the next generation more complicated (capital accounts to track)

# Limited Liability Company



- **Advantages**

- Ease of transfer
- Flexibility in defining relationships (how managed, how income is allocated, etc.)
- Limited liability protection
- Flexible taxation (can pick a lane)

- **Disadvantages**

- Formation costs (upfront work/expenses)
- Operation costs (have to comply with processes/regulatory requirements)

# Forming the LLC



- **File Articles with the Secretary of State**
- **Tradenname registration (if applicable)**
- **EIN if more than one member**
- **Operating agreement (defining the LLC's structure and role)**

# Example: Parents/Children



- **Parents create LLC**
- **Parents/children create operating agreement**
- **Parents transfer farm assets into LLC**
- **Children work/contribute assets – and increase percentage ownership over time.**
- **Over a set period, as circumstances dictate, children get 100% of the units.**

# The Operating Agreement: Key Elements



- **Contributions**
- **Allocations of Profits/Losses**
- **Distributions**
- **Management**
- **Liability**
- **Admission of new members**
- **Transfer of interests (ROFR/buy-sell)**
- **Dissolution**

# Common LLC Questions in Farm Transfers



- How will entering farmers pay for initial contribution?
- How will their share increase over time? How measured?
- How will the value of the interests be determined?
- Will voting rights correspond to % of ownership?
- What if the transaction stops making sense for one of the parties?
- Who makes decisions?
- How are disputes resolved? Is mediation required?

# Transfer of Interests



- Need to stay aware of and update annually or when a change is needed (the capitalization table). Common issue to capitalize, define the units, and not keep this up-to-date.
- Can assign interests, subject to limitations in the operating agreement, and often makes sense as an estate planning too.

# Example: Windswept Farmstead Cooperative LLC





# Corporation



- **Advantages**

- Ease of outside investment
- Ease of transfer
- Flexible taxation (could be an S corporation and pass through)
- Liability protection

- **Disadvantages**

- Formation costs (up front)
- Operational costs
- Tax consequences
- Potential for double taxation of profits (if C corporation) although tax laws have changed.

# Title to Land



- Tenancy by the Entirety
- Joint Tenancy with Right of Survivorship
- Tenancy in Common
- Life Estates (enhanced and irrevocable)
  - Establishes line of succession
  - Provides life income, but not impact longer-term ownership of the property.
  - Other factors:
    - ✦ Burden to hold/administer?
    - ✦ Difficulty in leasing? Only for lifetime of life tenant.
    - ✦ Probate? If the life estate isn't conveyed during lifetime.

# Estate Planning Tools



- **Wills**
- **Trusts**
- **Life Insurance**
- **Advanced Directives/Health Care Proxy/POA**

# Will



- **Advantages**

- Flexible (can modify or abandon until death)
- Very few restrictions on how can pass assets through will
- Can select an executor (to manage affairs)
- Avoid intestacy (where state law determines allocation of assets)

- **Disadvantages**

- Have to go through probate
- Could be a will contest
- Estate is a matter of public record
- Complications if assets in multiple states

# Elements of a Trust



- **Trust property**
- **Trustee**
- **Beneficiaries**
- **Management instruction/direction**

# Pros/Cons



- **Advantages**

- Avoid probate (or reduce)
- Fast transfer of assets upon death
- Avoid public disclosure of estate assets
- More difficult to contest

- **Disadvantages**

- Costs of formation (up-front expense)
- Can be complicated to transfer assets and retitle into the trust
- Layer of operational complexity
- Although revocable trusts are flexible during life, really stringent upon death

# Trust - Operation



- **Farmer transfers assets to trust**
- **Trustee has control**
- **Beneficiaries can use the assets as defined in the trust agreement.**

# Life Insurance



- **Advantages**
  - Avoids probate
  - Potential income stream to off-farm heirs
- **Disadvantages**
  - Upfront costs (cost to acquire policy and maintain starts immediately)
  - Investment yield may be less than other investments.



# Planning Tools



- **Advanced Directives/Health Care POA**
- **Financial Power of Attorney**

# Transactional Tools



- **Installment Contract**
- **Leasing**
- **Traditional Sale of Farmland**
- **Agricultural Conservation Easements**

# Installment Contract



- **Advantages**

- Immediate cash benefit.
- Potential tax planning benefit.
- Long-term relationship. Locks in title and the plan for the asset.
- May allow to transfer outside of bank financing (which may expand pool).

- **Disadvantages**

- Asset tied up for years.
- Defaults back if payment missed (may lead to unanticipated consequences)

# Leasing



- Trial run to define relationship. This can potentially include options to purchase.
- Leasing plays a prominent role in many transfer structures.

# Traditional Sale of Agricultural Land



- Involves down payment with buyer lining up equity financing (and mortgage) for the remainder of the purchase.
- Advantage: immediate payment and transfer.
- Disadvantage: immediate loss of control and potential tax implications from lump-sum sale.

# Transfer Issues



- **Environmental**
- **Conservation Easements**
- **Zoning and Local Permitting**
- **Septic**
- **Taxes**
- **Current use**
- **Wetlands**
- **Title defects/need for survey**

# Agricultural Conservation Easements



- Possible tool to enable farm transfer (potential monetary or tax benefits).
- Option to Purchase at Agricultural Conservation Easements.
- Drafting considerations/coordination with lenders.

# Questions?

