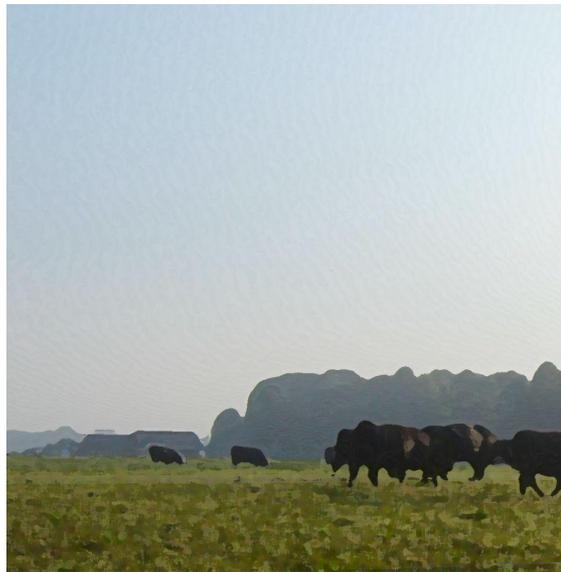


Farm Law and Tax for Producers and Landowners

The Flexible Architecture of Farm Succession: Disposition, Management and Options

Robert Andrew Branan, JD • rabrana2@ncsu.edu



NC STATE UNIVERSITY

Farm Law and Tax for
Producers and
Landowners

This Legal Educator's Background

- Member of the Virginia State Bar (1992) and North Carolina State Bar (2003)
 - Non-profit work in agriculture (2002 - 2009)
 - American Farmland Trust
 - NC Farm Transition Network
 - Private (Farm) Law Practice (2008 - 2018)
 - NCSU Agricultural and Resource Economics (2018 -)
 - 50% Extension appointment
 - 50% Teaching (Environmental and Agriculture Law)
 - Agricultural Law (4 year NCSU undergraduate)
 - Environmental Law and Economic Policy (4 year NCSU undergraduate)
 - Agribusiness Law (2 year Agricultural Institute NCSU program)
- » Curriculum Coordinator, April 1, 2025

<https://farmlaw.ces.ncsu.edu/>

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Conservation Easements: Save the Date for Three Part Series, September 7, 14, 21

Please join this series of webinars on September 7, 14 and 21 at 1 p.m. for an update on ...

FEATURED



Farm Ma NCSFMR Shenand Agricultu

In the last we North Carolina and Rural App

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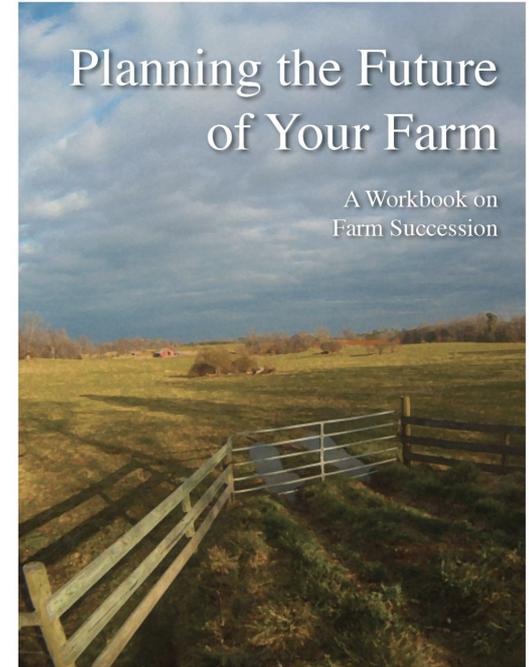
So You Inherited a Farm

Topics and Templates Concerning Transfer and Management of Interests in Farm and Forest Land



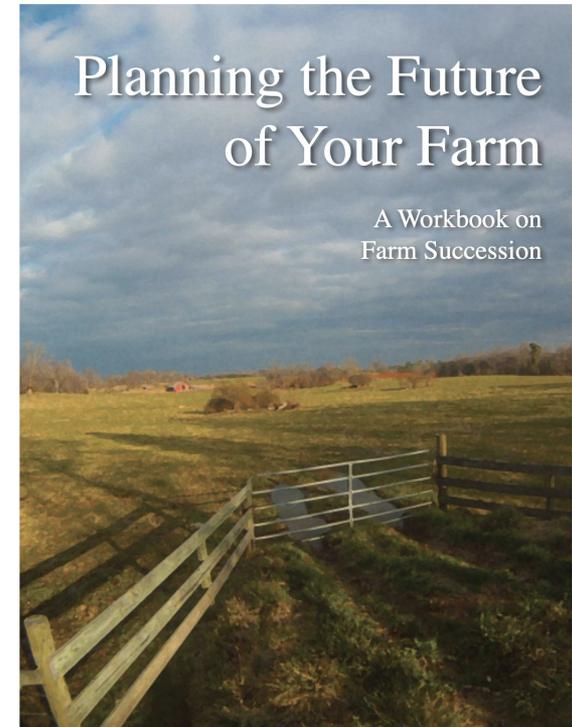
Planning the Future of Your Farm

A Workbook on Farm Succession



Projects: Planning the Future of Your Farm *Revisited*

- Grant from NC Tobacco Trust Fund
- Implement form of survey from FARMTRANSFERS project
- Deliverables:
 - survey/consult activity with commodity groups
 - update of PFYF workbook
 - WHY? because it is 7 years since last update and still in use
- components as Extension fact sheets
- **The Ask:** please respond to my email if you are connected with a group and can



Recent Study on Farm Succession

[Factors Impacting Succession Planning](#) (Lippsmeyer, M. et al., Purdue University (quotes))

- Our sample of 403 farmers across the United States indicates that implementation of succession plans for farms **is largely unrelated to operator age**
- Examining specific management practices, **68%** of farms with written succession plans use **written lease agreements** compared to just **52%** of farms without succession plans
- Farms with succession plans tend to use **financial ratios and standard operating procedures**, evaluate crop pricing performance, operate larger farms, are more resilient to strategic risk, and their operators are more highly educated.
- ... significant and **positive correlations between succession planning and balance sheet strength**; the establishment of goals, objectives, and core values; and farms looking for opportunities that new enterprises may provide.

This Legal Educator's Observations

- Try not to give heirs undivided interests in land
 - property law is indifferent to your goals for the land
- Estate Tax exemptions still high, but will sunset end of 2025
 - election results likely ensure “permanency” at current exemption levels
 - taxes should not be the focus of farm succession, but influence design
- All land dispositions must be in writing... saying “all this will be yours” means nothing
- Careful of PUV property tax when dividing land
- “Legacy” planning is a series of disposition decisions and executions
- Secure Option Agreements whenever possible (in leases, entities, etc.)

If real property (land) has a “change in use” appraised value, may have to subdivide and distribute

Multiple Goals of Succession...

“Keep land in the family” (preserve legacy)

“Preserve wealth, avoid taxes”

“Provide equal wealth for family members”

“Live in comfortable retirement”

“Keep a ‘going concern’ business in operation”

“Provide farming opportunity” (for family or community)

“Ensure land is never ‘sold for development’”



This Legal Educator's Guiding Principles

“Planning is everything. The Plan is nothing.” - attributed to Gen. Dwight Eisenhower

“You can't paper over people” - Leon Geyer, Virginia Tech

“If you can't make it perfect, make it flexible” - Pullet Grower, Chatham County

“Be mindful of leaving legacy obligations behind” - R.A. Branan, NCSU

Property Disposition Tax Implications

- **Sale** of property: **Capital Gains Tax** (FMV-Acquisition Value) \times ~15%
- **Gifting** of property:
 - Carry-Over Basis (potential higher capital gains tax)
 - Gift Tax (for annual gifts above \$18,000 [per donee])
 - Lifetime gift tax exemption: \$13,610,000
- Property at **Death**:
 - **Estate Tax**: percentage tax levied by law on all wealth transferred at death (aka “taxable estate”)
 - Subject to “**Wealth Exemption**”
 - **Federal Exemption = \$13,610,000 per individual (federal only) (spouse gets other exemption for double)**
 - “Unified” with lifetime gift tax exemption (dollar for dollar, above annual exclusion of \$18,000/yr/donee)
 - Estate tax abolished in North Carolina
 - Probate costs: percentage levied by county on **personal property** wealth (aka “probate estate”)

Current Law: Gifts and Basis

Gift Tax Exclusion Amounts for tax years beginning after December 31, 2017 and before January 1, 2026:

- Annual Exclusion \$18,000 (2024)
- Lifetime Exemption (2024): **\$13,610,000** (\$27,220,000, married couple)
- Carry-Over Basis (donee gets same basis as donor)

Step-up basis to Fair Market Value is retained for death time transfers

- New basis at time of death, reduces capital gains if sold by 'heirs' (see [IRC §1014](#))

Example Gift: Land purchased in 1985 at \$1500/acre, current FMV \$8000/ac

- if gift and donee sells, capital gains/acre: $(\$8000 - \$1500 = \$6500) \times 15\% = \985

Example Death Transfer: Same basis, FMV \$8500 at date of death

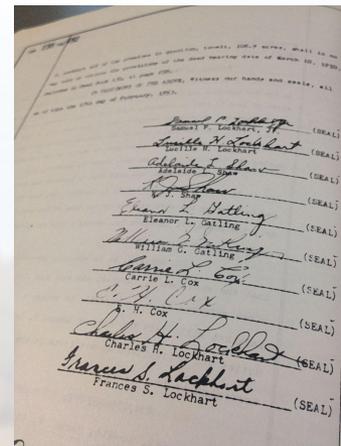
- if death transfer and donee sells, capital gains (with modest appreciation)/acre: $(\$8700 - 8500 = \$200) \times 15\% = \$30/\text{acre}$ capital gain

Can still *defer* capital gains with §1031 "like kind" exchange (e.g. land for land)

Still have LLC valuation discounts and §2032A valuation reduction for qualifying farms

Capital Gain Income

- Tax rate variable, 0%, 15%, 20% depending on income tax bracket
- **Rate** applied to appreciation (difference between **sale price** and **basis**)
 - e.g. **15%** x (**\$100,000** - **\$85,000**) = \$2,250
- Long term asset sales
 - Real Property (land)
 - long term assets
 - Timber sales
 - Stocks held ≥ 1 year
- [IRC §1231](#)



Deferment of Capital Gain: §1031

Generally, for tax years beginning after December 31, 2017, like-kind exchanges are allowed for real property that is not held primarily for sale (inventory)

- Must set up prior to closing, identify **qualified intermediary** to hold the sale funds
- Must identify exchange property within 45 days of closing on relinquished property
 - May identify up to 3 properties with listed values, OR
 - any number of properties but combined not exceed 200% of property sold ([26 CFR § 1.1031\(k\)-1](#))
 - Must close on 95% of the properties identified
- Must close on replacement property within **180 days** of closing on relinquished property

Absorbing Shocks (a/k/a the 6 “D’s”)

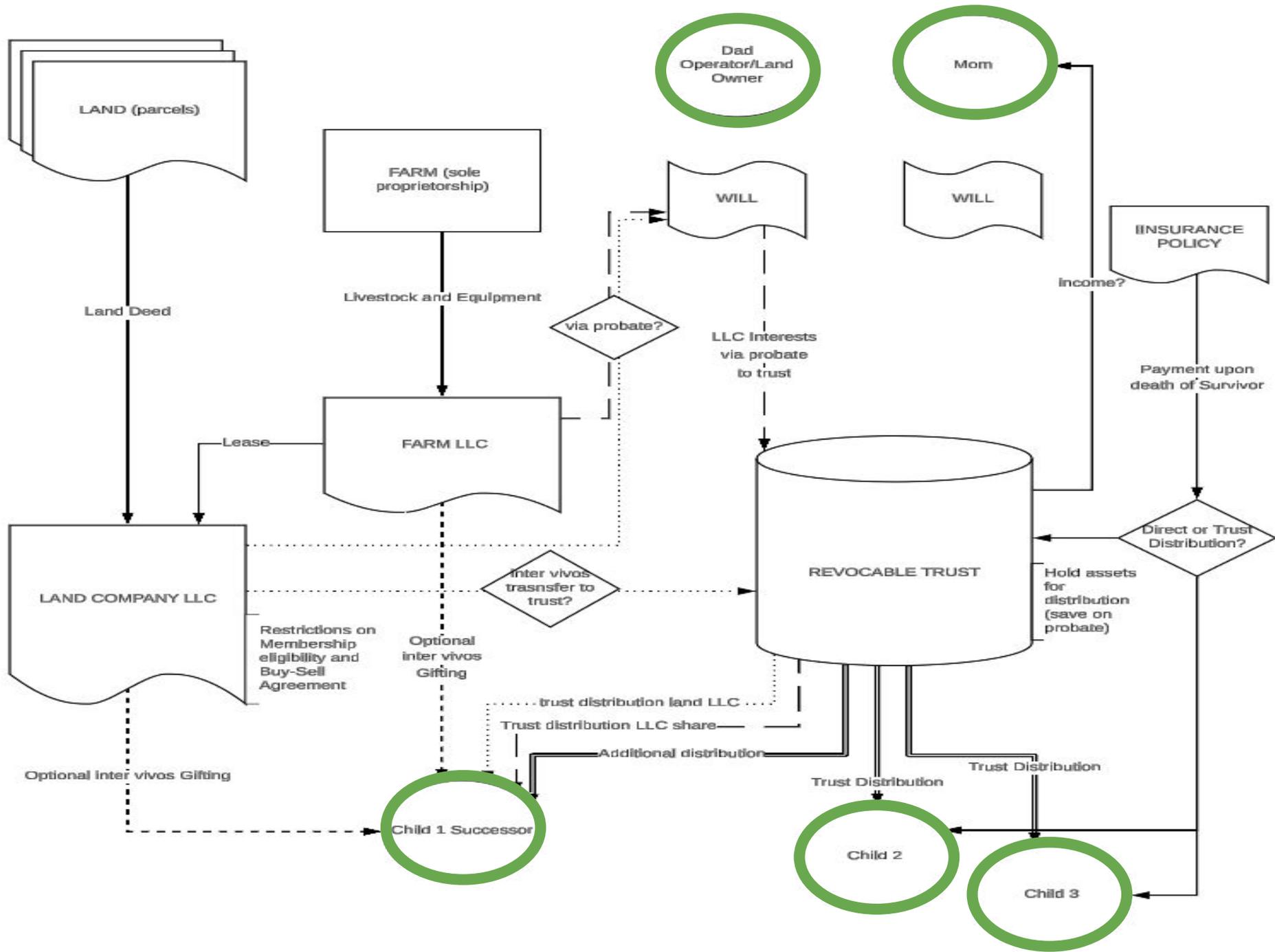
- **Death**
 - how are assets disposed at death of interest owner? (**will and trust**)
- **Disability**
 - contingency for management in event of disability (**LLC operating agreement, powers of attorney**)
- **Divorce**
 - ensuring that a business or land interest stays ‘in the family’ (**LLC operating agreement**)
- **Disaster**
 - crop failure, unmanageable debt, bankruptcy (**LLC operating agreement, crop insurance**)
- **Disagreement**
 - framework for decision-making power and dispute resolution (**trust, LLC operating agreement**)
- **Disenchantment or Departure**
 - impact on ownership of business and assets (and property disposition decisions) (**trust, LLC operating agreement, purchase options**)

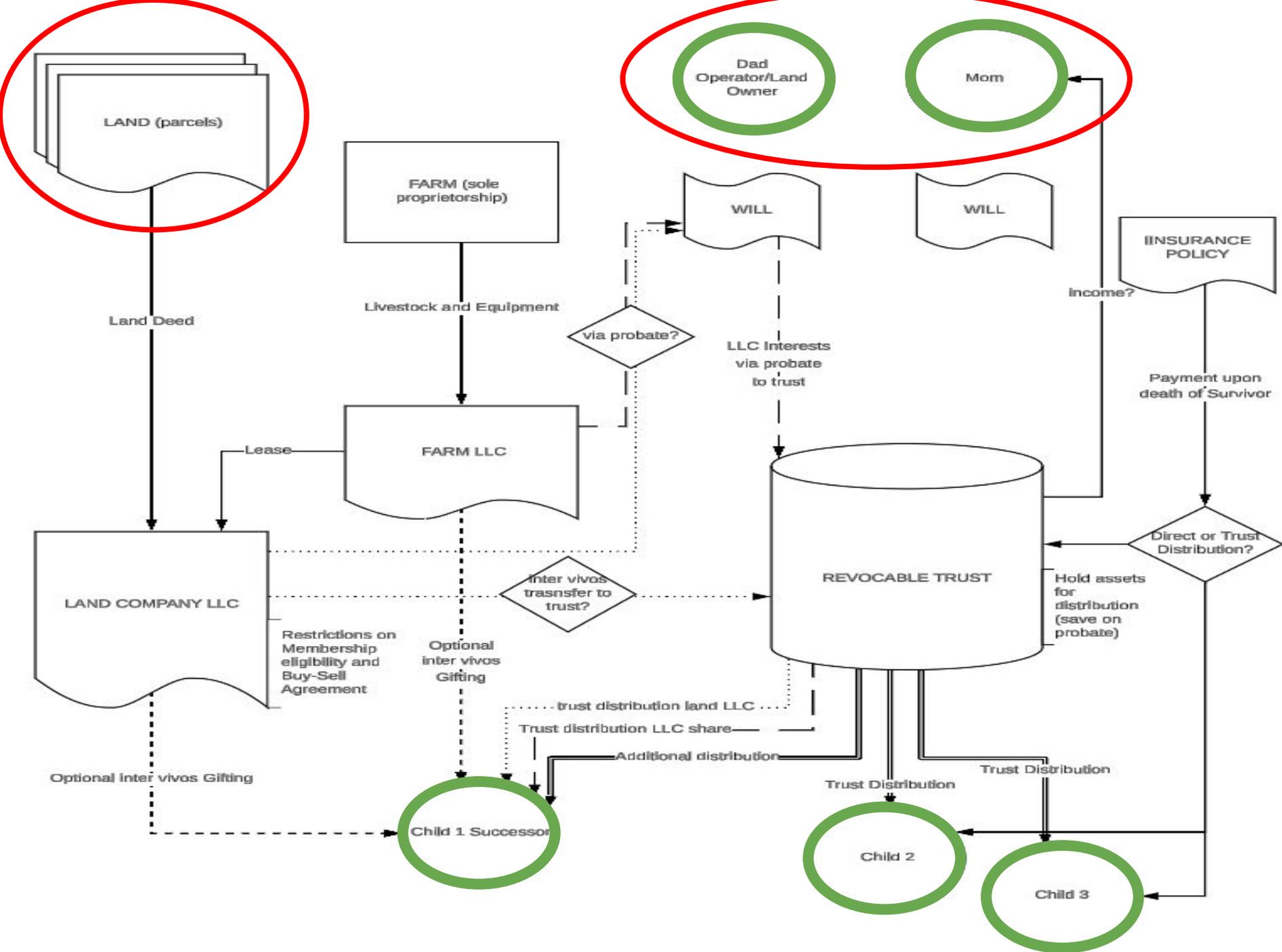
Scenario One

- Dad has built farm operation up over years
- Dad has inherited land
- Dad has purchased land jointly with Mom
- Dad operates as a sole proprietorship, married filing jointly
- Son has come “back” after college to work on the farm
- Son has two sisters who have moved away from the home farm
- Assumption: there is enough available land to lease in the area to increase total acreage









Agency: Powers of Attorney

- A written document, signed and notarized
- Where an adult person (the “principal”) assigns his or her rights and powers over **property** to another person, called an “**attorney in fact**”
 - “Attorney in Fact” acts in the shoes of Principal
 - Sell property, take loans, make financial dispositions, etc.
- 1. **Durable Power of Attorney:** powers of attorney in fact over property ‘survive’ the incapacity of principal
 - Requires recording with Register of Deeds
 - **Power ends at death of Principal**
- 2. **Health Care Power of Attorney:** Principal empowers another to make medical decisions for him or her if cannot directly communicate with healthcare providers
 - can contain a Do Not Resuscitate command
- 3. **Living Will** or Advance Medical Directive: **speaks directly to** healthcare providers regarding decision to end life support
 - Takes decision away from anyone other than physician

Real Property 101: Land Title

- Fee Simple: owned by one person
 - Life Estate
 - “Owner A for life, remainder to B”
 - **Tenancy in Common**
 - Alienable and undivided interests
 - **Joint Tenancy**
 - Joint Tenancy with Rights of Survivorship
 - A modern rarity
 - Tenancy by the Entireties
 - may become joint property by deed (H to H + W)
 - Spouse may have rights to inherited property at owner’s death or divorce (must claim, not automatic)
 - **Inherited land is not joint (or marital) property** [\[NCGS 50-20\(b\)\(2\)\]](#)
 - still subject to elective share [\[NCGS 30-3.1\]](#)
 - still subject to life estate election [\[NCGS 29-30\]](#)
-
- [Land Title: Understanding Rights in Property](#)
 - [The Property Rights of Surviving Spouse](#)
 - [Present Use Value: Transferring Property Enrolled in Present Use Value Property Taxation](#)
 - tk: prenuptial agreements



“The Bundle of Sticks” (all severable)



**Riparian (surface)
Water Rights**

(e.g. Deed to adjacent parcel right to draw surface water)

**Right to
Subdivide**

(e.g. Deed to land trust in form of conservation easement)

**Right to Take
Wildlife**

(e.g. leased to hunting club)

Right to Farm

(e.g. Leased to farmer)

Right of sole possession

(e.g. deeded right of way/easement to utility)

**Right to
Timber**

(e.g. timber deed to timber buyer)

**Right to
Groundwater**

(e.g. shared with another entity or parcel)

**Right of sole
possession**

(e.g. deed of access easement to adjacent parcel)

**Right to
subsurface
minerals**

(e.g. Deed to energy developer)

**Right to
transfer/control equity**

(e.g. Deed of Trust to lender)

Only Three Ways to Dispose of Property

- **Sale**

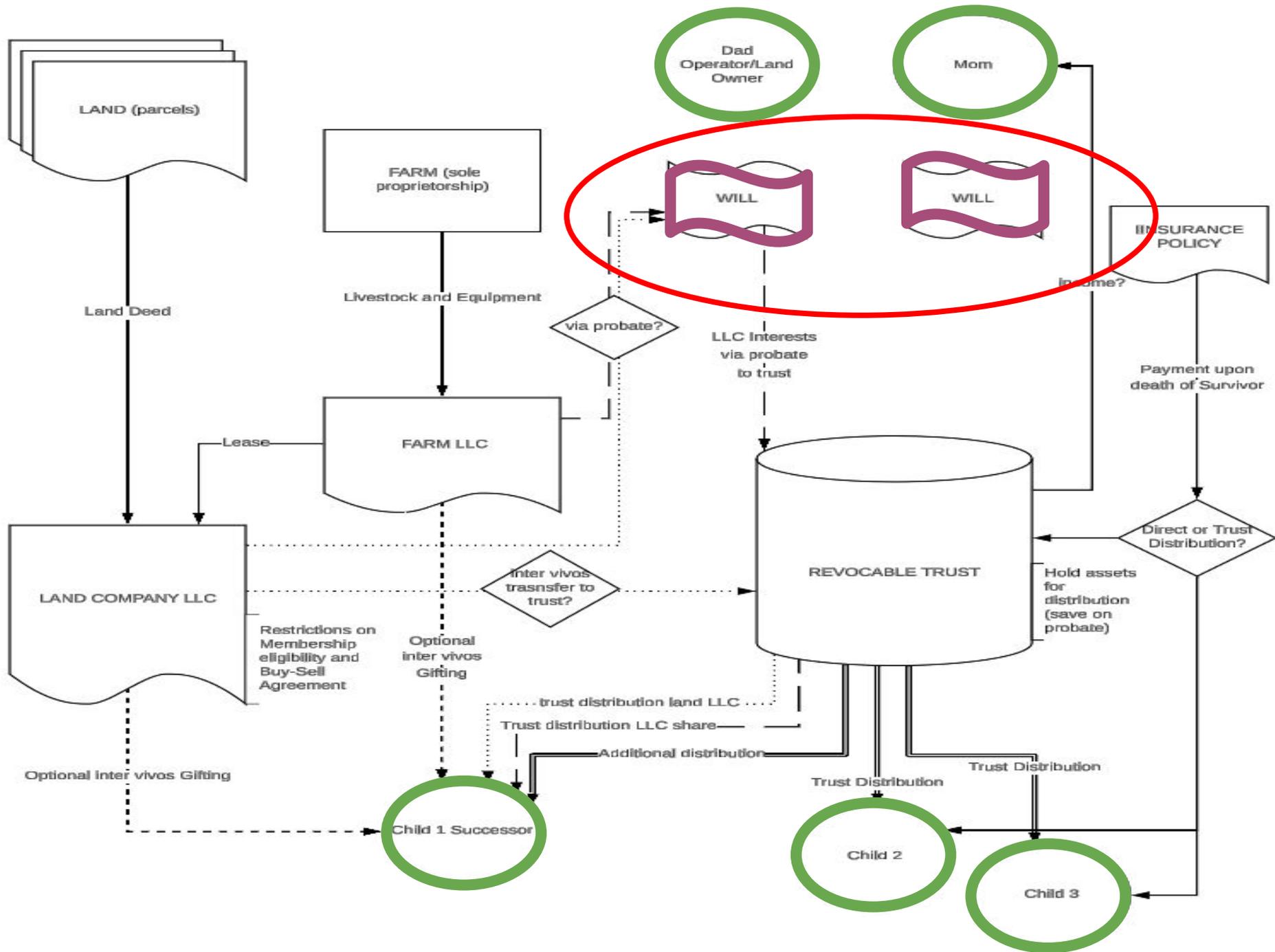
- Completely relinquish rights in property, receive fair market value in cash or equivalent (aka consideration)
- May reserve rights (timber, an easement, etc.)
- Tax consequence: capital gains on sale income

- **Gift**

- Completely relinquish rights in property, nothing in return
- Tax Consequence: Carry-over basis

- **Death**

- Property interests pass to heirs at law (intestate) or legatees (testate - personal property)/devisees (testate - real property)
- Tax Consequence
 - Subject to federal estate tax
 - Probate fee (not a tax) percentage of personal property value in probate estate (excludes survivorship property, property already in trust, etc.)



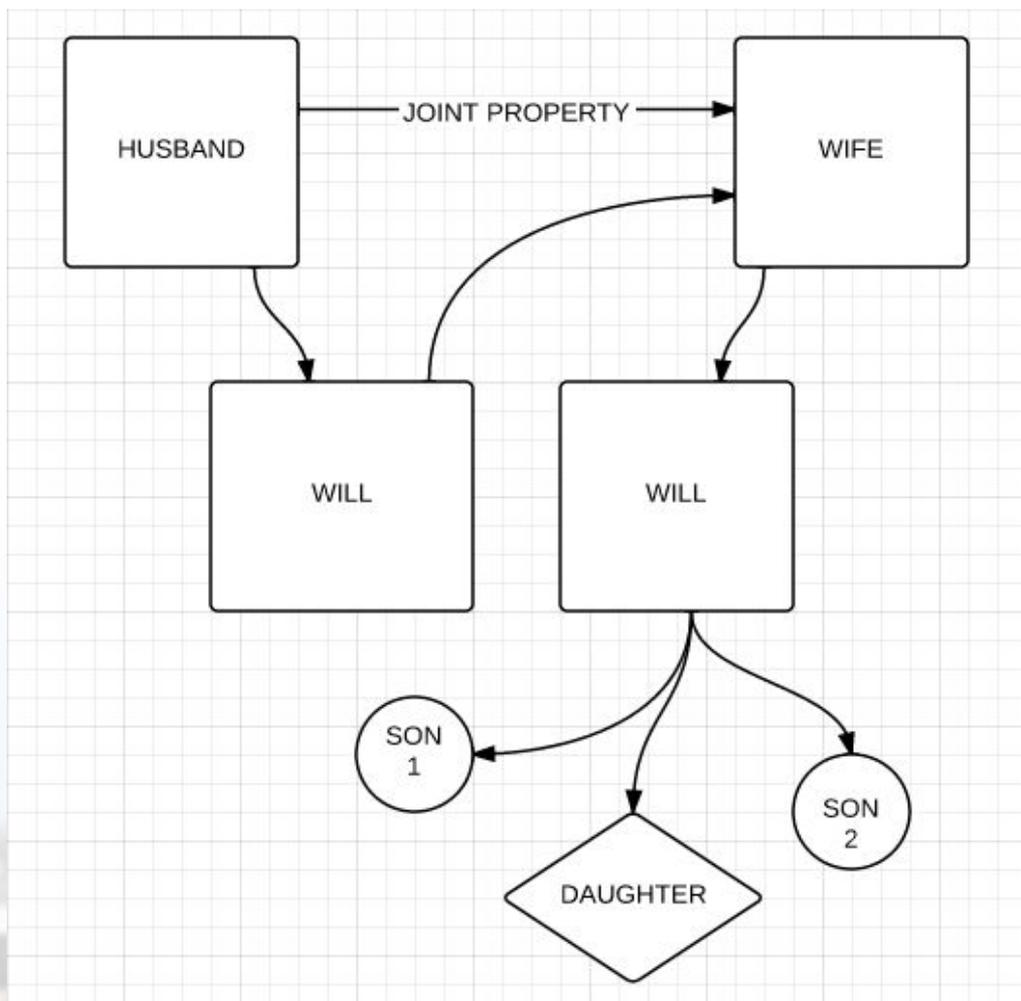
Disposition at Death

- **Testate:** person dies (decedent) with a valid will
 - late 15c., from Latin *testatus* "public, manifest, published"
- **Intestate:** person dies without a valid will, property is distributed according to **Intestate Succession Act** ([N.C.G.S. Chapter 29](#))
 - Distributions to spouse, lineal descendants, lateral descendants, or ancestors depending on facts at moment of death
 - Spouse % varies with # of children or grandchildren
 - Children and grandchildren (% varies by class)
 - Siblings and parents (depends on whether lineal descendants alive)

Creating a valid Will

- Requirements codified N.C.G.S. § 31-1
- Testator (age 18+) must have mental capacity
 - Understand you are making a will
 - Understand Nature of property you own
 - Understand Who you are leaving it to
- **Testator must sign**
 - In the presence of two “disinterested” witnesses
 - Have no inheritable interest under the will
 - **Self-Proving Will:** Testator and witnesses sign in the presence of a notary public
 - With no notary, Clerk must call in will witnesses to testify as to validity of signature
- **Holographic Wills:** written and signed in handwriting of testator ([N.C.G.S. § 31-3.4](#))
- **Clerk must decide if will meets legal sufficiency for entry into probate**
- **Intent of Testator Controls!**
- [The Last Will and Testament: A Primer](#)

Typical Reciprocal Will scenario



“All property to spouse”

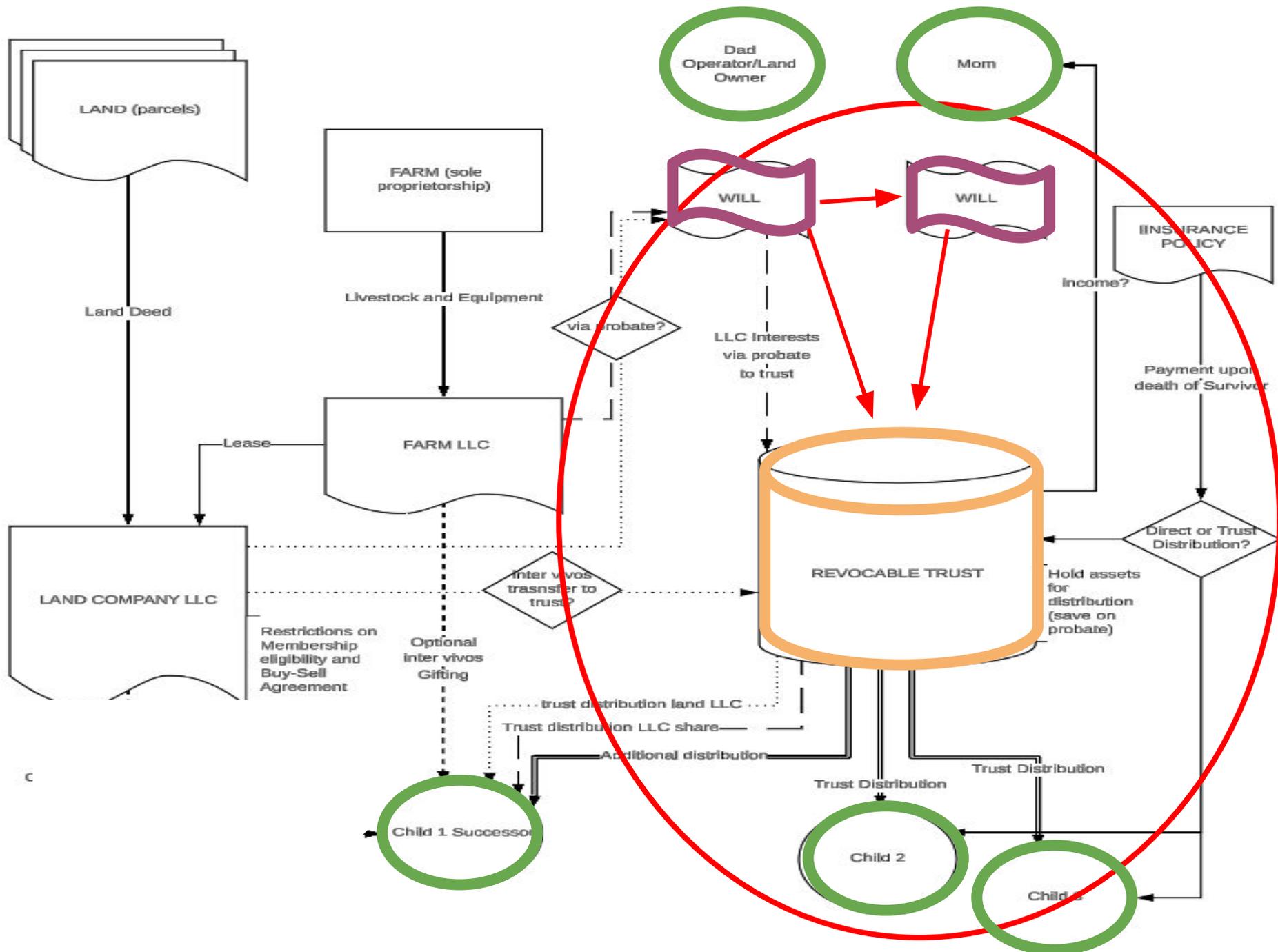
“If predeceased by spouse, to children share and share alike, *per stirpes*”

When surviving spouse dies:

Son 1: $\frac{1}{3}$ all property undivided

Son 2: $\frac{1}{3}$ all property undivided

Daughter: $\frac{1}{3}$ all property undivided



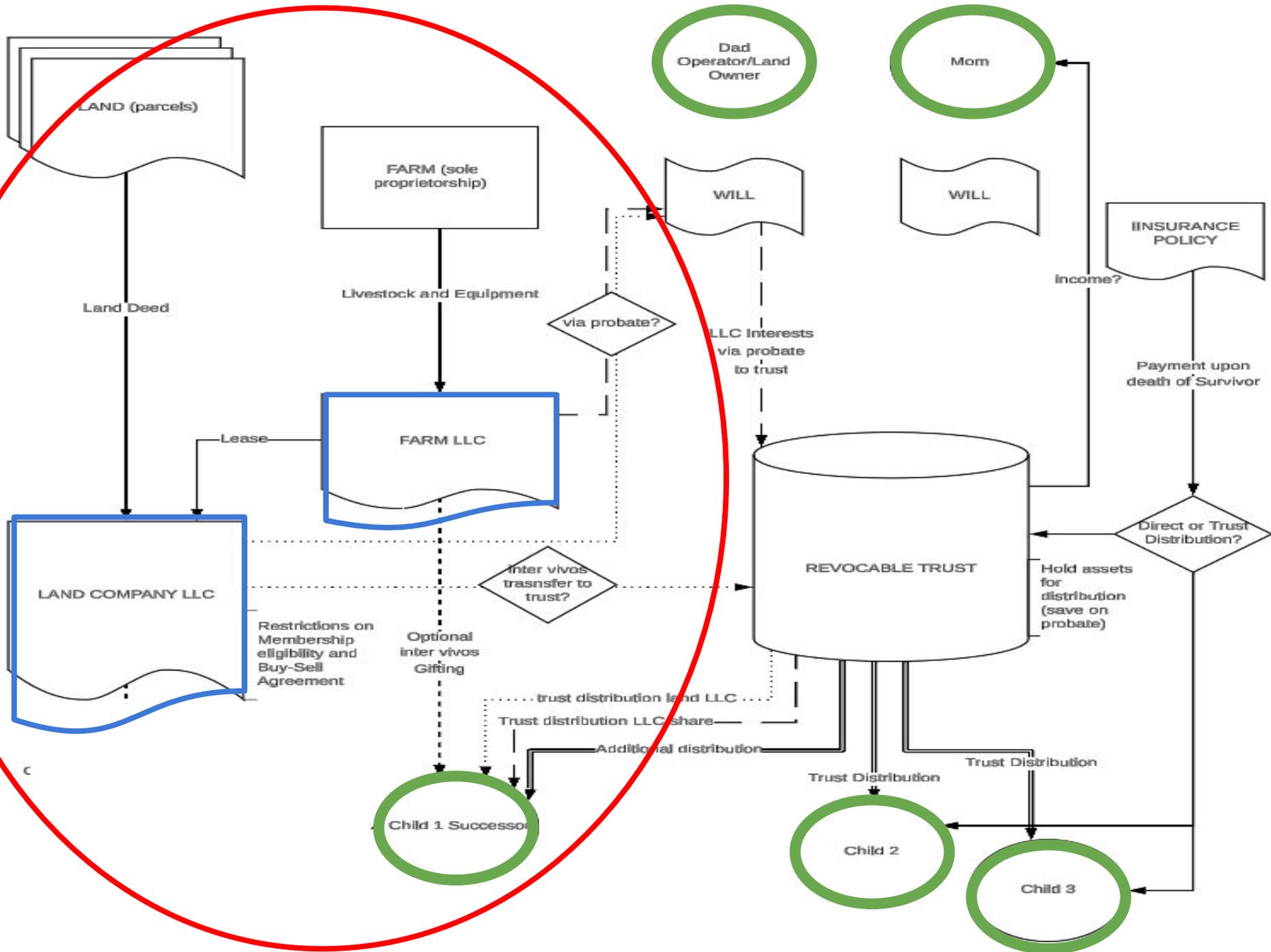
The Trust

- A separate legal entity
 - NOT a potential intestate heir
- **Settlor** (or Grantor): the person(s) who create(s) the trust and funds it (assigns property to the trust)
- **Trustee**: the “legal owner” of the trust property, bound by a fiduciary duty (state law) and by terms of the trust
 - **Fiduciary powers of trustee** [NCGS § 36C-8-816](#)
- **Beneficiary**: The person(s) who receive the benefit of the trust
 - income from assets
 - distribution of assets
- **Language of the Trust controls distribution**
- Trusts are private, **assets not part of probate estate** (but part of taxable estate if trust was revocable)
 - Often used as “will substitutes”: trust determines distribution of property
- **Can empower Trustee to place conservation easement, place land in entity, require leasing for farming, etc.**
- **[The Basics of Trusts in Farm Succession Planning](#)**

General Types of Trusts

- **Testamentary Trust** (established by executor pursuant to a will)
- **Revocable Trust**
 - Fund during lifetime (put in, take out)
 - Fund through ‘pour over’ will
 - Amend as needed
 - [Table of Contents Example](#)
- **Irrevocable Trust**
 - Insurance Trust (ILIT)
 - “Asset-Protection”
- Special Needs Trust
- Charitable Trusts
- “Dynasty” Trusts
 - Revocation of “rule against perpetuities”





Use of Business Entities

- Business Entity Interests
 - Governing document (e.g. Operating Agreement) controls disposition of interests in entity
 - The Buy-Sell Agreement (option, valuation (purchase price, payment))
 - Business Entity interest (shares, membership) = **intangible personal property**
 - **Gifts of interest to create equity in younger generation**
 - Land titled to business entity = personal property
- May transfer interests in business entity to successors by gift, sale or at death
- [Limited Liability Companies: Steps in Formation](#)
- [Sample Asset Contribution List](#)

Use of Business Entities

- Liability protection (protect personal wealth, land)
- Organization of business assets
 - e.g. equipment, input inventory
- Contract between owners
 - determines rights in management and income
 - ultimate disposition of assets
- Possible vehicle for reducing parents' estate value
 - Valuation discounts under IRC regulations
 - Organized gifting or sale program (annual transfer)
- Can use multiple entities for large farm management
 - **USDA “payment limitation” structure**

Limited Liability Company

- Operating LLC (or S Corp)
 - Partners contribute their ownership interest in cattle, bins, machinery, “sweat” etc.
 - Use as transfer vehicle to farming heir (gifts/structured sale)
 - Existing S Corp or Partnerships (merger, conversion, asset transfer, etc.)
- Land LLC
 - Deed Land interest to the LLC (*never* a corporation)
 - Restrict membership
 - Strip partition rights inherit to real property interest
 - Structured exit of equity in land (title substitute)
 - Conversion of existing Limited Partnership (w/o retitle property) (SOS filing)

The Operating Agreement

- A **Contract** between contributors of assets
- Restricts who can be members
 - Member vs. Assignee
- Dictates voting requirements for decisions
 - Manager
 - Voting and Non-voting Units
- Dictates triggers for buy-sell
 - **Farming Heir Option to Purchase**
 - Who may buy and when
 - Appraisal procedure
 - Price and payment terms (seller finance option)
- For existing S Corps, use Stock Purchase Agreement
- [Limited Liability Companies: Operating Agreement Components and Sample Language](#)
- [Buy Sell Agreements - Options to Purchase](#)

Intervivos Transfer of LLC Interests

- Gift of Interest (measured in “units”)
 - Calculate value of company
 - Divide value by number of units to determine price per unit
 - Transfer total units < \$19,000 annual gift tax exclusion
- Sale
 - Purchase from Other Members or Trust
 - Purchase with insurance proceeds under Buy-Sell Agreement (Designate beneficiary and agreement between all participants + spouses)
 - Spread capital gain over term note
 - Discounting of interest value
 - Some relief from Self Employment taxes

Suite of Templates for LLC Unit Transfer Regimen (PFYF annotated docs)

[Valuation of Units](#)

- Calculation of “tax-excluded” transfer
- Ledger of ownership (noting certificates of ownership)

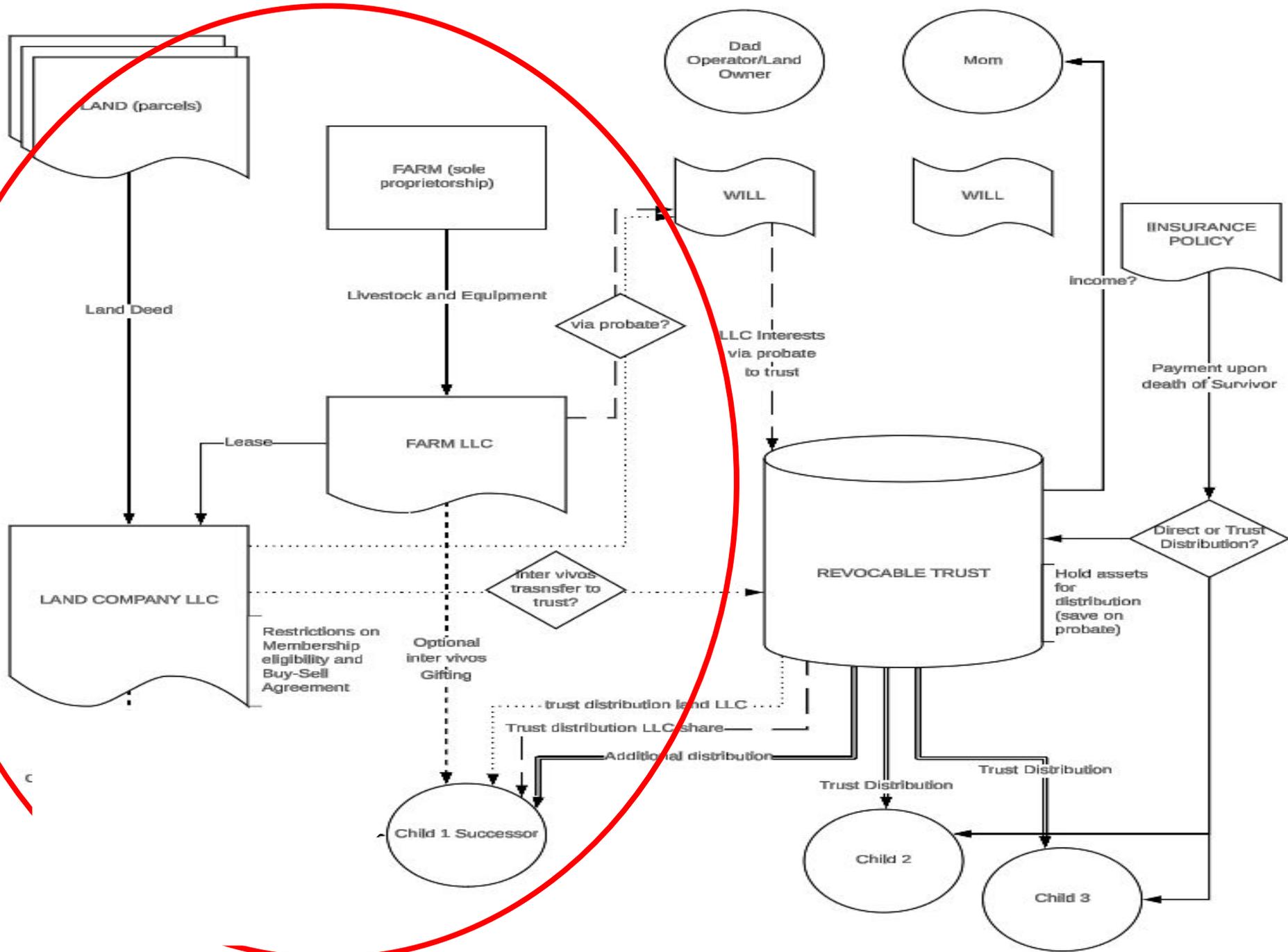
[LLC Member Resolution](#) to Add Member, Transfer Interest

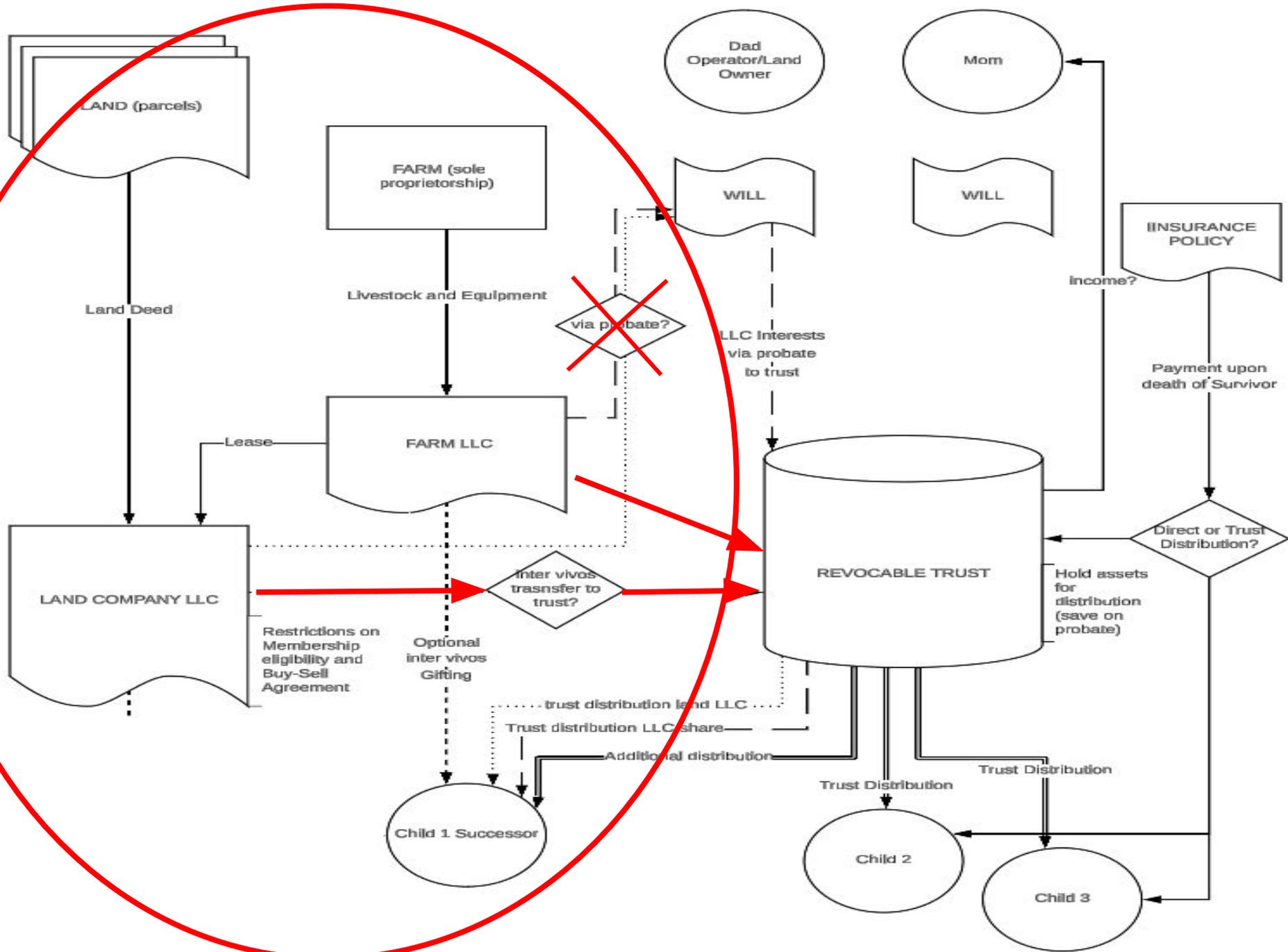
[Declaration of Gift](#)

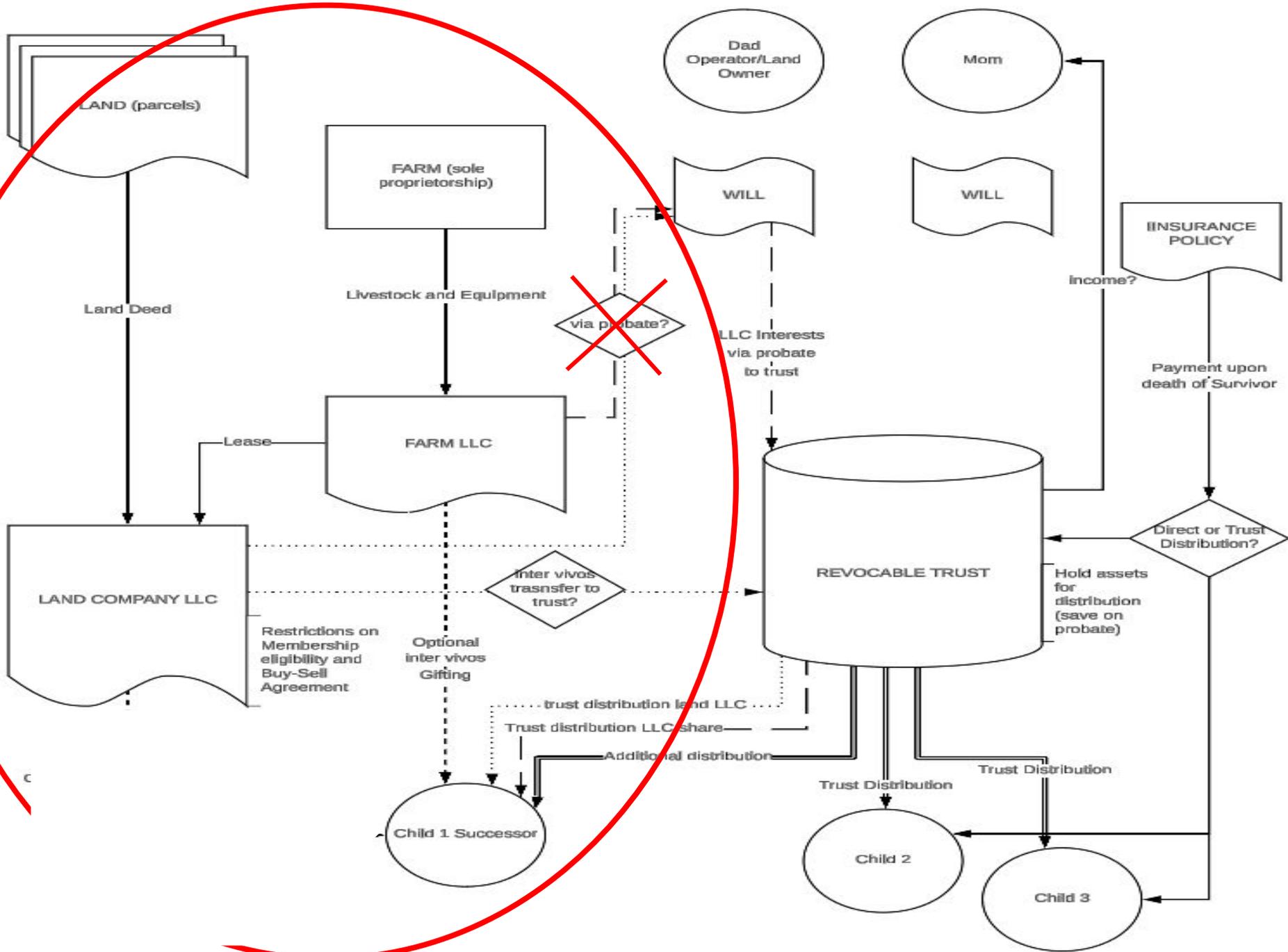
[Unit Certificates](#) and gift endorsements

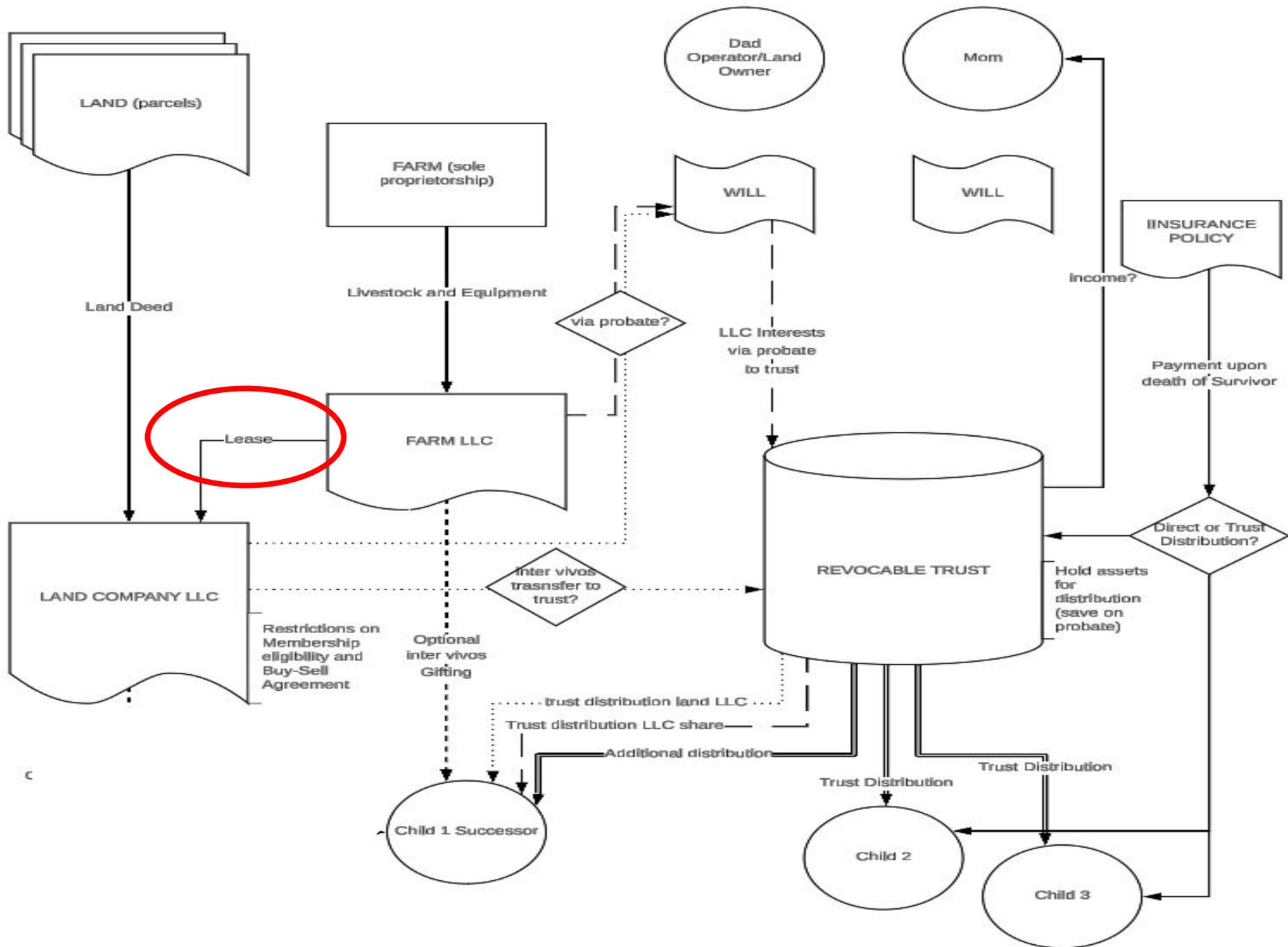
[Operating Agreement](#)

- PFYF working document for annotation









Lease Considerations

- Basis for Agreement
 - Landlord and tenant will meet with their own ideas
 - And then meet in the middle
- Legally enforceable vs. Practically enforceable
 - Note what you want to leave with
- Cash rent amount
 - market difficult to discern (closely guarded secret)
 - “\$35/acre/year in Chatham County”
- Crop Share
 - not as common in North Carolina (?)
 - “farming on fifths” (?)
- Farm Management Agreement?
 - Paying the tenant?
- Consider options for purchase
- **Must record terms 3+ years (protect against sale)**
- Farm Law page: [Leases and Farm Tenure](#)
 - [The Verbal \(Statutory\) Farm Tenancy](#)
 - [Leasing Considerations for Farmers and Landowners](#)

Option Agreements

- Contractual “foot in court house door”
- Must be recorded in County Register of Deeds
 - by memorandum (form in NCGS)
- “Right of First Offer”: must negotiate prior to listing property
- “Right of First Refusal”: less advantageous, optionee has leeway to entertain highest offer
- May be embedded in lease
- Set **appraisal procedure**, and process for reconciling competing valuations
- [Option Agreements for Purchase of Land](#)

Going Concern Business Valuation

Formula Terms

- Going concern value: Price willing to pay (\$Y) for a business if, based on that amount, purchaser will earn a future stream of income valued at (\$X) annually?
 - $Y = \text{historical gross income stream (discounting unusual events)} \times \text{growth percentage (trend)}$
- **EBIDTA = Earnings Before Interest, Taxes, Depreciation and Amortization = cash flow**
 - Buyout price will reflect this figure (for a certain # years into future)
 - Annual sales revenue x “industry multiplier”
- **Brand Value**
 - **Trademark** or brand name
 - Visual assets such as a logo or brand colors
 - Unique marketing strategy
 - Digital assets or licenses
 - **Level of customer loyalty**
 - Key to valuing a local farm business



Valuation of Assets: Appraisal

- Comparable Sales Method
 - What have other properties sold for in the area (real property)
- Cost Approach
 - Replacement cost of asset (normally applied to personal property)
 - Valuation of Machinery: take list (with year and make) to an equipment dealer
- County tax appraisal for land
 - **good enough for planning**

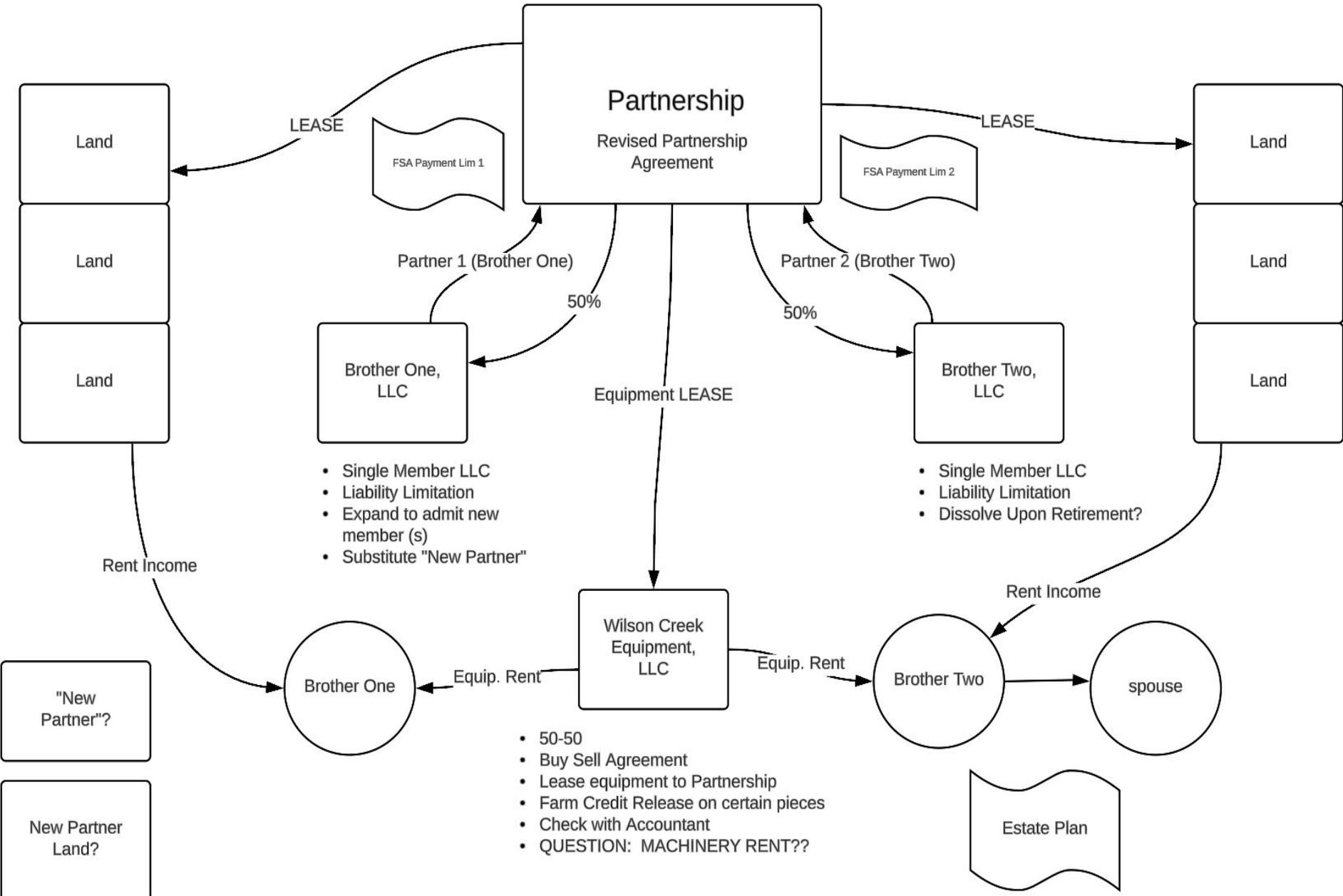


Care in Using Devices

- The Will
 - title passes at moment of death
 - **unless specific property devises/bequests**, property passes by class
 - e.g. “To my children”: 3 children
 - 3 parcels of land, farm equipment/livestock, personal property
 - each child takes $\frac{1}{3}$ co-tenancy interest in land, $\frac{1}{3}$ interest in all personal property
 - Executor (and Clerk of Court) without authority to decide who gets specifically what
- The Trust
 - must choose a trustee
 - not ideal as long-term landowning device for farmland (rent may be insufficient to cover costs)
- The LLC - the family members are ‘in business’ with one another
 - cannot “paper over people”

Scenario Two: Brothers Partnership

- Two brothers
- inherited land from parents
- each has purchased their own parcels
- farm has large equipment portfolio
- Younger brother divorced
- Older brother married, thinking of retirement
- Younger brother has son interested in joining in future
- Significant acreage, need to maximize farm bill payments



2018 Farm Bill Payment Limitations

Program	Limitation
Combined PLC and ARC payments	\$125,000 per crop year
Noninsured Crop Disaster Assistance (NAP)	\$125,000 per crop year
Market Facilitation Payment	\$125,000 per person

“Actively Engaged in Farming”

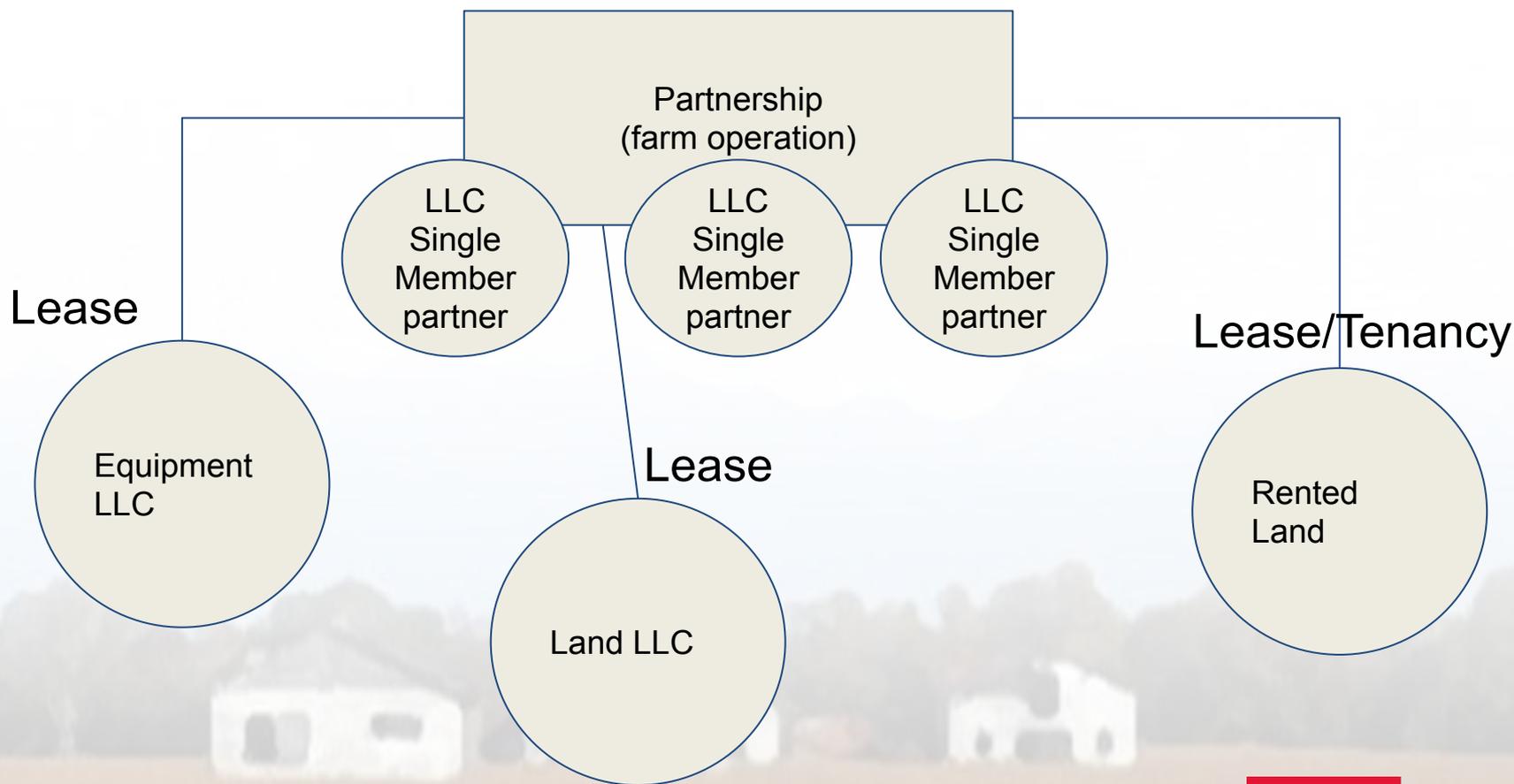
- “Family Farm” adults (18+ years) of common lineage deemed AEF (ascendants, descendants, siblings, spouses) ([7 CFR 1400.208](#))
 - 2018 Farm Bill now includes first cousins, nieces, and nephews (reference)
 - Landowner exception for share crop situations (reference)
- Three AEF criteria (all)
 1. The person, independently and separately, makes a significant contribution* to the farming operation of (a) capital, equipment, or land; **and** (b) active personal labor, active personal management, or a combination of active personal labor and management.
 2. The person’s share of profits or losses is commensurate with his/her contribution to the farming operation.
 3. The person shares in the risk of loss from the farming operation.

* defined in [7 CFR 1400.3](#)

Entity Payment Limits

- Corporations and LLC = one payment
- All members must be AEF that is identifiable, documentable, separate, and distinct from the contributions made by any other partner
- If a member is not AEF, then payment reduced by percentage of that owner's share
- Partnership comprised of multiple entities
 - Each LLC is a partner, each gets a payment limit

Basic Model: Partnership Addition



Discussion Scenario

- Philip and Elizabeth (60's) have four children (30's) (Charles, Andrew, Anne and Edward)
- Parents own 900 acres of land (in 12 parcels)
 - 50% farmland
 - 50% timber and wetlands
- Philip operates row crop operation, tobacco, etc. and livestock
 - farms 450 owned acres, 3000 rented acres
 - ~ \$1M in equipment
 - land used as collateral for operating loans
 - Charles is by farm most involved the operation

Suggestions

- Organize farm operation into Partnership with individual LLCs
 - preserves USDA payment limitations
 - this serves as ownership and management transfer vehicle
 - Philip can make gifts of ownership to Charles
 - operating agreement provides framework of management, disagreement, etc.
 - LLC becomes tenant to P & E's land (and other owners)
 - LLC gets long term lease (?)
- Evaluate land resources (try even distribution in values)
 - best farm land to Charles
 - other farmland and timberland to other children, (perhaps Charles has option to purchase or right of first refusal)
- Purchase life insurance to provide inheritance for uninvolved children
- Place land in Trust (or pour to trust through Will)
 - trustee distributes parcels upon death of survivor of P & E
 - any LLC interest owned by P gets to C

THANKS FOR INVITING ME!



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