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Planning Today for Tomorrow's Farms

A Workbook *for* Tennessee Farm Families

The University of Tennessee
Institute of Agriculture

Foreword

The objective of this workbook is to provide readers a solid foundation upon which they, and all of the people involved, can understand basic farm and forest succession planning concepts and processes. Of equal importance, this workbook seeks to prepare all of the individuals to effectively search for and use the appropriate professional services required for the development of a high-quality farm succession plan.

Throughout, this workbook assumes that the farm transfer will take place between two families, related or unrelated, and that their business relationship will continue over an extended period. However, the information contained in the manual is certainly applicable to a wide range of situations.

Successful farm succession planning takes a comprehensive approach that involves all of the planning categories discussed below. Given the potential for each chapter to be used independently, some information may be reiterated in several chapters. Lastly, this manual is meant to be used in conjunction with the Web site www.farmlandlegacy.org where updated chapters, additional references and information on upcoming conferences and training will be continually added.

The workbook is organized as follows:

Chapter 1: Why Succession Planning? – This chapter introduces the basic concept of succession planning and provides insight as to why succession planning is so important to farm families and Tennessee's agricultural sector.

Chapter 2: The Family Discussion – This chapter examines the critical importance of communication in the farm succession process.

Chapter 3: Taking Stock of Your Estate – This chapter guides the process of generating records for succession planning as well as those needed for improved decision making.

Chapter 4: Business and Organizational Structure – This chapter presents the various options for structuring a farm or family business and describes the factors that should be considered in choosing a particular structure, including how the structure fits into a succession plan.

Chapter 5: Estate Planning Tools – This chapter covers wills, trusts, powers of attorney and other documents and information for developing an estate plan to transfer assets to the next and future generations.

Chapter 6: Acquiring Professional Services – This chapter provides guidance on identifying, choosing and working with professionals, such as attorneys and accountants, to formulate and execute a succession plan.

Chapter 7: Retirement Planning – This chapter presents available options and emphasizes the need to plan properly for retirement.

Glossary – This section provides definitions for key words found throughout the workbook.

Additional Resources – This section lists a variety of resources that may be of use to families involved in succession planning.

Appendix – This section contains worksheets to assist you with developing your succession plan. The worksheets are referenced throughout the chapters and are organized accordingly.

Legal disclaimer

The materials in this workbook are provided for educational purposes only. While workshop presentations and the materials in this workbook involve issues of a legal nature, they should not be relied upon as legal advice, nor should these materials be used as a substitute for the services provided by a qualified legal or other professional familiar with your individual circumstances.

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Chapter 1: Why Succession Planning?

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Agriculture is often thought of as an intergenerational venture and one that is handed down through the generations. Farm family members are integrated into the enterprise early on, fulfilling age-appropriate chores. Eventually, 'pitching in' evolves into actual employment and a means of generating income. A ***principal operator*** or a core group of family members often serve as the key decision makers, therefore risk bearers, and likely run/own the business – depending on the structure. As these key family members age, day-to-day responsibilities may shift, but ownership often remains a much stickier situation.

Although the intent may be to hand the family farm venture down from generation to generation, the devil is in the details. The situation becomes even more challenging if realizing your dream of ensuring your farm's legacy is complicated by the lack of interested family members or those whose vision does not align with yours. In addition, many family farms are a relatively complex mix of relationships, business structures and revenue streams that make planning and succession challenging, as well as precipitating a need for professional guidance.

With this in mind, you have probably decided to pick up this workbook because you want to have some peace of mind about where your farm and farm family are going to be in the future. This manual is designed to assist you and your farm family as you go through the planning process necessary to position yourselves for a successful transition of your business. Though not a comprehensive resource, this manual aims to prepare families who own businesses to seek the appropriate professional assistance that is often required to build a farm ***succession plan***.

You Are Not Alone

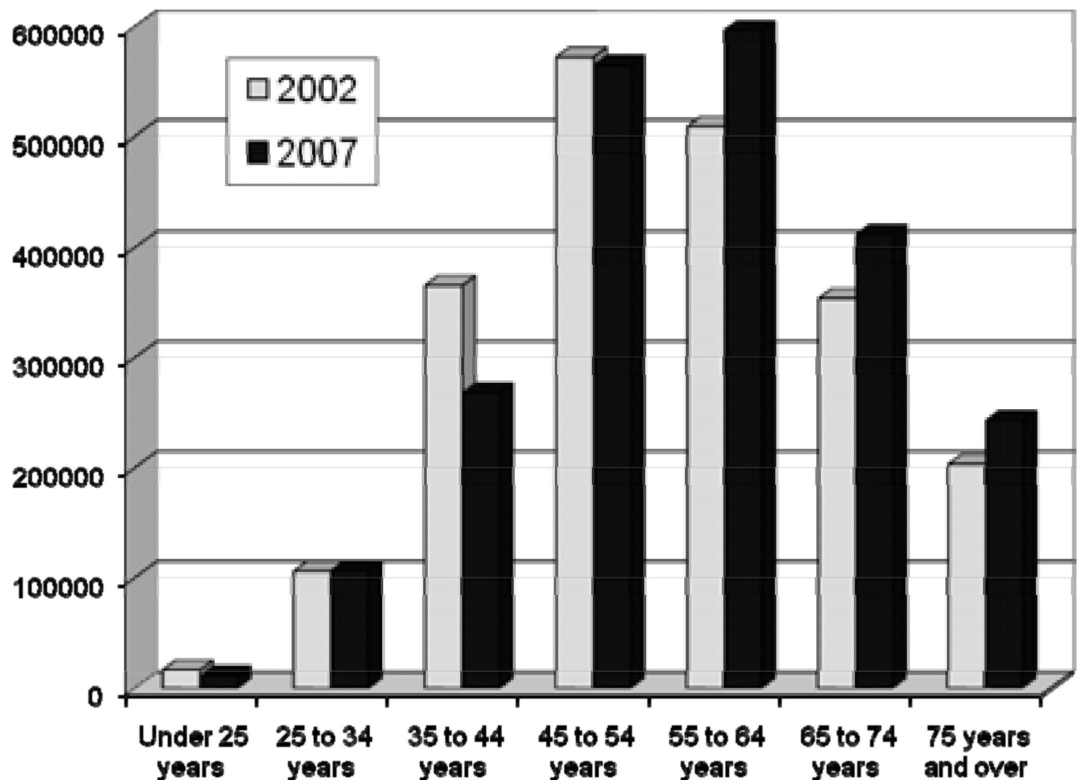
If you have just started thinking about the long-term future of your family farm, you are not alone. A recent study suggested that 55 percent of adults in the United States do not have a will[1]. In agriculture, the situation may be far worse. *Farm Journal*, a popular farm magazine, recently did a survey of its readers to find out more about their succession and estate plans. Almost 80 percent of the respondents plan to transfer control of their operation to the next generation, but fewer than 20 percent are fully confident of their succession plan.[2] These survey results are cheerier than a recent study quoted by the

FarmLASTS Project[3], which found that 88 percent of farmers and farmland owners neither had an exit plan nor knew how to develop one. In addition, of the farmers planning to retire, only about 30 percent had an identified successor. Given all of these statistics, it is easy to understand why the Small Business Administration has found that family businesses have less than a 33 percent chance of survival between the transition from the first to second generation ownership, and only half of those businesses survive the second to third generation transition. This leaves roughly 16.5 percent of family firms surviving to a third generation of ownership.[4] Inadequate succession planning is one of the biggest threats facing most small businesses, including farms.

Farmers are Older and Farming Longer

We constantly hear about the aging or "graying" of the farm population and the numbers support this statement (see charts on next page). However, this aging is mostly due to older farmers exiting at a slower rate alongside a declining rate of new farmers entering the agriculture sector[5]. In fact, between 2002 and 2007, the number of principal operators (farmers) above the age of 55 grew 17 percent, while the number of principal operators under the age of 45 fell 21 percent (Figure 1.1). The result is that the average age of farmers continues to increase and the majority of U.S. farmland remains under the control of farmers over the age of 55. This means two things for farmland transfers: there are less of them in a given year than in the past and these older farmers may be more resistant to developing a succession plan, perhaps given the weighty financial considerations and emotional stress. Ultimately, these demographic shifts emphasize the need for succession planning as farms remain under the control of an increasingly older generation. Without proper succession planning, land use, agricultural production and rural economic development issues will likely arise.

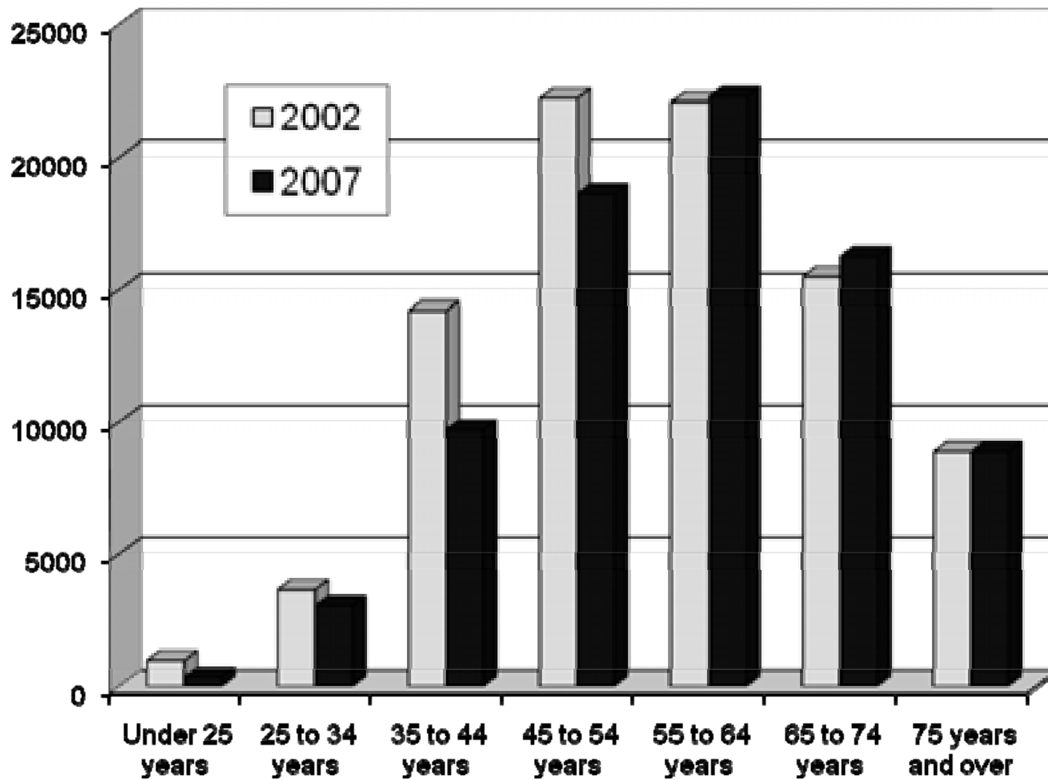
Figure 1.1: Number of Principal Operators in United States, by Age Range, in 2002 and 2007



A Look at Tennessee

The situation in Tennessee is very similar to the rest of the United States. Farm succession continues to weigh on principal operators who, as a whole, continue to retain farm ownership as they get older (Figure 1.2). As the older generation retains ownership, the number of farms in Tennessee has decreased by 9 percent and land in farms has decreased 6 percent since 2002 (Table 1.1). The aging of Tennessee's farmers implies considerable changes in farm management and ownership over the next decade. These changes pose risks to the continued operation of family farms and to the ability of new and beginning farmers to acquire farmland. In fact, 61 percent of all Tennessee farmland is controlled by an operator who is more than 55 years old. In contrast, only 15 percent of Tennessee farmland is controlled by an operator less than 45 years old.

Figure 1.2: Number of Principal Operators in Tennessee, by Age Range, in 2002 and 2007



Data source: NASS, 2009a[6]

Table 1.1: Number, Average Age, Gender and Primary Occupation of Principal Operators in Tennessee, 2002 and 2007

Item	Principal operators (2002)	Principal operators (2007)	Percent Change
Operators (number)	87,595	79,280	-9%
Average age of operator (years)	56.0	57.8	3%
Gender of operator \ male	78,182	69,320	-11%
Gender of operator \ female	9,413	9,960	6%
Primary occupation \ farming	44,100	30,849	-30%
Primary occupation \ other	43,495	48,431	11%

Data source: NASS, 2009a[6]

In addition to age, the primary occupation of the principal owner is of interest. Nearly two-thirds of principal operators in Tennessee work off-farm as their primary occupation (Table 1.1). This is especially true among principal operators who are less than 65 years old. However, it is interesting to note that principal operators who work primarily on-farm and are over the age of 55 own the majority of farmland. This has implications on land availability and farm transition. For new agricultural ventures, if land remains tied to the older generation, land availability will be an issue. And, though the farm may contribute to the livelihood of the family in many important ways, primary off-farm employment signals an important non-farm source of income, potential access to additional retirement planning tools (e.g.., 401(k) or 403(b) plans) and other considerations that may significantly affect farm succession planning on either end of the generational spectrum.

The evolving role of women in agriculture:

Implications for farm succession planning

A closer look at the current demographic trends for principal operators in Tennessee underscores the importance of farm succession planning. Between 2002 and 2007, the number of principal farm operators declined as farm numbers declined. However, this result was driven by a proportionally larger loss of male operators **versus a net gain** of female principal operators (Table 1.1). Though they only represent 12.6 percent of principal operators, women represent 28.8 percent of all operators in Tennessee. In fact, women more than 55 years old represent the fastest growing demographic for operators in Tennessee! Female operators are of interest because women play a significant role in the financial management and decision-making aspects of their family farming operations.

For more information see NASS, 2009b[7].

Women and non-traditional succession. Historically, first-born male children were often identified as successors. Now, a growing percentage of farmers are identifying daughters as potential successors. Fewer new farmers are acquiring farms from family members and more beginning farmers are coming from non-farm backgrounds. What was once tradition is evolving – as is everything in agriculture. As they say, “It’s not your grandpa’s farm anymore.” In fact, “traditional” succession – passing from older to younger generations within the family through purchase, gift or inheritance – accounts for only half of farmland acquisitions.

Farm Succession and the Future of Agriculture

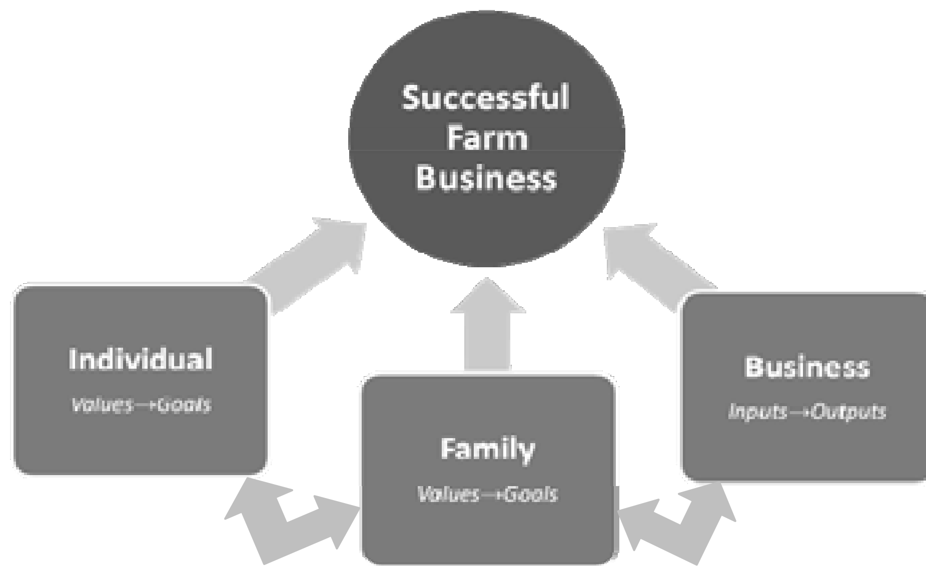
According to the 2007 Census of Agriculture, the market value of Tennessee's agricultural products was $2.6 billion, which placed Tennessee 33rd in the country. However, this does not take into account the entire agricultural value chain. Menard et. al. (2009) note that in 2006 the entire agro-forestry sector contributed $78.9 billion to Tennessee's economy and employed more than 502,000 individuals.[8] Therefore, who controls these businesses and how they transition in ownership over time could have a significant impact on Tennessee, not just on the farm family seeking to prepare for the future.

The future of agriculture in the U.S. and in Tennessee relies on the ability of older operators to exit without losing their farm to development, taxes, poor planning and/or family disputes, in conjunction with the ability of new farmers to overcome the challenge of gaining access to affordable and productive farmland. In other words, the future of agriculture depends, in part, on successful farm succession planning between current and future generations of farmers. This can be in the form of farmland transfers between two generations of family members or between two unrelated farmers working together to aid in the exit of one and the entry of the other. Lastly, approximately 70 percent of U.S. farmland will change hands in the next decade[3], further underscoring the need for succession planning if we are to 'Plan Today for Tomorrow's Farms' in Tennessee.

Farm Succession Planning Overview

A successful family farm business is a composite of many different elements (Figure 1.3). First, a family farm is combination of individual human resources (skills, health, abilities) and family social resources (the bonding and trust between farm family members and the bridging across families). In addition to individuals and their families, the family farm has business inputs – natural (land/climate), financial, built (buildings, capital, infrastructure) resources that can be transformed into marketable outputs (products and services). Ultimately, the goals of the family farm are based on these resources, and the values that guides their use. In other words, the "mission" of the farm is a result of individuals, their families and available resources. Successful ventures develop a robust mission statement around these elements and seek to run efficient operations that effectively adapt to external influences affecting product demand, supply, costs and other important factors.

Figure 1.3: Elements of a Successful Family Farm Business



No matter how successful or well-run a farm business might be, the owners will eventually contend with how to address succession. Succession is defined as the act or process of one person taking the place of another. Farm succession planning is essentially planning for change in farm business ownership from one person to another. However, it is more complex than it might seem.

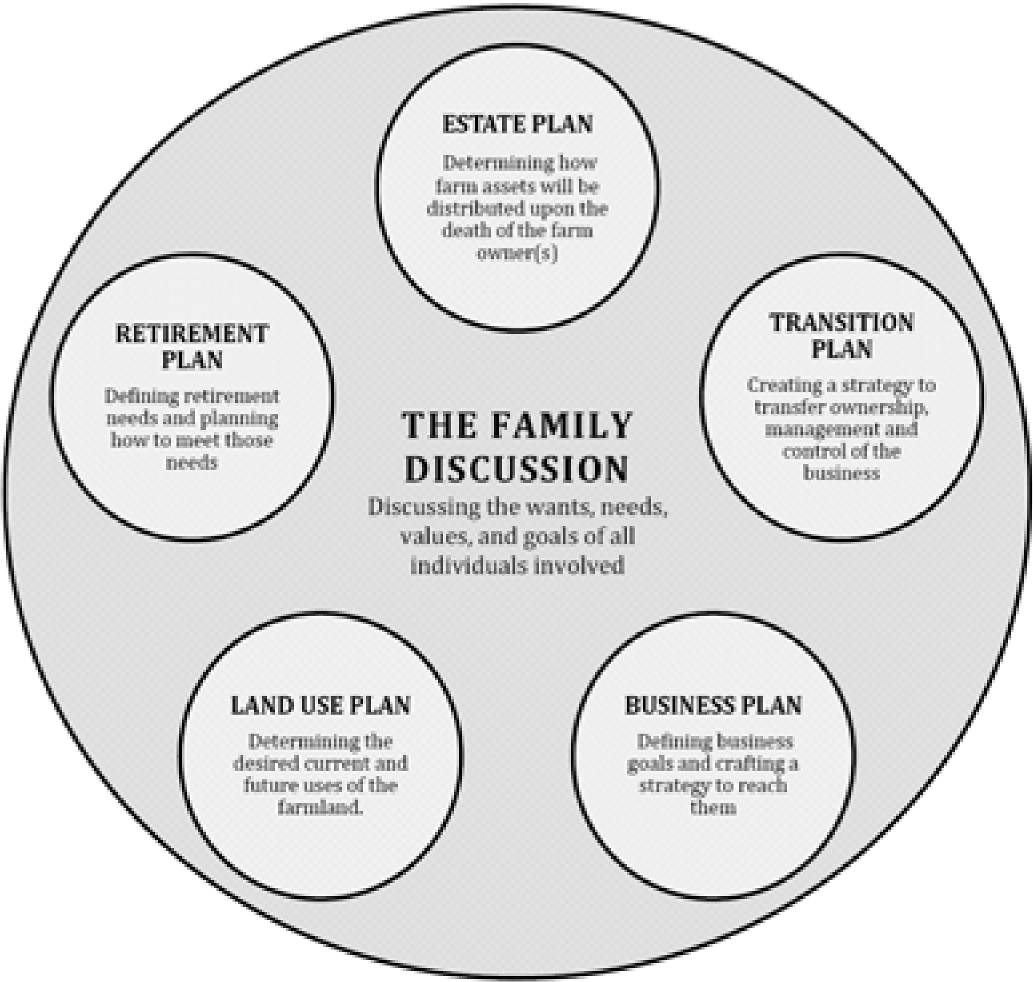
Farm succession planning is a continuous process that involves transferring knowledge, skills, labor, management, control and ownership between generations. This workbook captures this process through inclusion of the following elements (Figure 1.4):

- **Retirement Plan**: Defining retirement needs and planning how to meet those needs;
- **Estate Plan**: Determining how farm assets will be distributed upon the death of the farm owner(s);
- **Transition Plan**: Creating a strategy to transfer ownership, management and control of the business;
- **Business Plan**: Defining business goals and crafting a strategy to reach them; and
- **Land-Use Plan**: Determining the desired current and future uses of the farmland.

It is important to note that communication is at the heart of every well-designed and successful succession plan. Communicating the wants, needs, values and goals of all

individuals involved is a pivotal first step. However, it is imperative that communication be an ongoing element of any succession plan. Succession plans do not happen overnight. As days go by, the opinions and desires of those involved in the planning may change. Maintaining constant and transparent lines of communication will increase the probability of successful succession planning. When communication is front and center during each step of the plan design, needs and wants will be openly addressed and the pathway to a successful conclusion will be more completely understood by all.

Figure 1.4. The Farm Succession Plan



A Word of WARNING!

Often the most overlooked part of a farm succession plan is the transition plan. Part of the transition plan is the transfer of management, which is a process, not an event, and may take years to complete. The transition plan should involve mentoring and shifts in responsibility from one owner to the next over an agreed-upon period, the length of which depends on the complexity of the operation. Most commonly, the only part of a succession plan that is completed or focused on is the estate plan, which only transfers the ownership of assets. This is dangerous. If you simply give ownership of a car to a 16-year-old without driving lessons, it could lead to a disaster. The same holds for businesses. If you only transfer the tractor, livestock, barns and land to the next generation without teaching them how to manage the operation, your farm legacy could be short-lived. Just as the 16-year-old will know how to drive safely after lessons, a young farmer who has time to learn how to manage the farm will know how to operate a successful farm business.

Why Should You Plan for the Succession of Your Farm?

Like many rural businesses, family members typically run farm businesses. These businesses, reminiscent of the family members who own the farm, typically go through a predictable lifecycle (Figure 1.5) with four basic phases: start-up, growth, maturity and decline.

Start-up: The goal of the business in this phase is survival. Survival depends primarily on the ability of the owner to maintain cash flow, overcome new challenges through innovation and sustain confidence and enthusiasm about the future of the business.

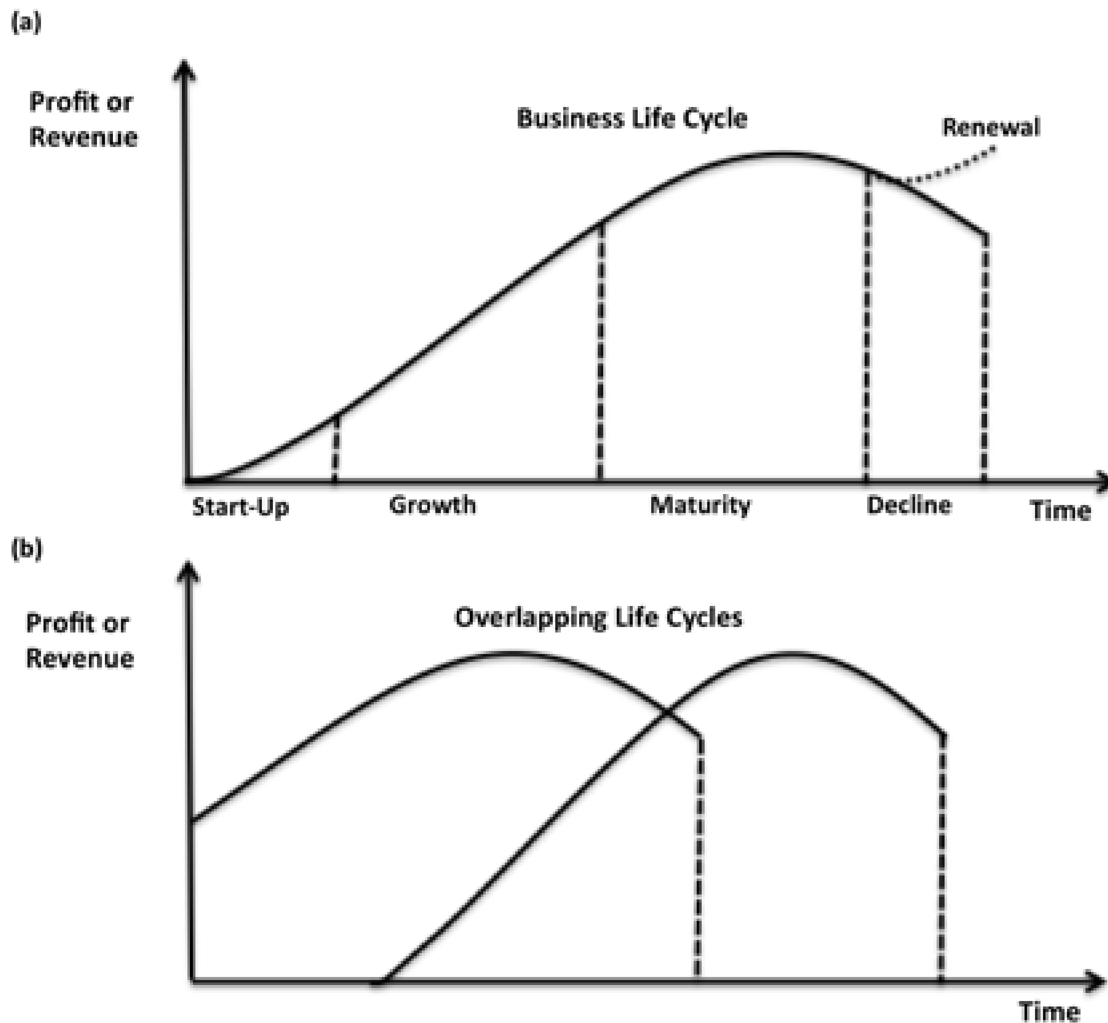
Growth: Survival of the business generally leads to growth. During this phase, the owner focuses on expanding production and sales. As the owner continues to develop his or her managerial skill set, he or she begins to delegate responsibilities in an effort to develop and implement new products/services or management strategies to sustain growth. Cash flow and available investment capital may still constrain efforts.

Maturity: This phase is the point where ownership and leadership begin to intermingle. As a leader, the owner uses managerial skill to steer the business toward greater efficiency during this phase of profits and relative stability. At this point, the business has reached a sustained level of sales and a full complement of employees. Now that the pieces are in place, the owner may begin struggle with complacency and the business with lack of innovation.

Decline/Renewal: Successfully meeting the demands of starting and sustaining the business often means business owners in this phase typically rely on the infrastructure

already in place. Getting to this point takes time, and many owners find themselves thinking about the future of the business. Inaction may result in the eventual decline and ultimately, termination of the business. Proactive planning may serve to revitalize the business, as employees and the eventual successor begin to lay the groundwork for a new era.

Figure 1.5: (a) Typical Business Life Cycle, (b) Business Life Cycle with Overlapping Generations *(Adapted from Hofstrand, 1998 [9])*



For farming businesses, these stages are closely tied to changes in human, built and financial capital. The skills and experiences of the successor, especially if he or she is a family member with close ties to the farm, have been built on years of experience helping out and possibly working as a paid employee on the farm. Oftentimes, the

successor has also received applicable training at a school, college or university. This human capital provides a foundation for succession. However, nothing surpasses actually being mentored by the current owner. As many have found out the hard way, agriculture is as much art as it is science. Overlapping lifecycles allows the successor to learn the intricacies of the farm. Not only will this relationship be beneficial for knowledge transfer, but this will also be an opportunity for the owner and the successor to support one another. For example, the owner will be able to offer the financial and management support that is often lacking during the successor's start-up and growth phase. The successor may serve as an important source of labor and innovation that is in short supply in the owner's maturity and decline phase. These complementary phases are the source of the "Renewal" in Figure 1.5.

Another goal of farm succession planning is to ensure that farm assets – primarily land and improvements (natural/built capital) and financial capital – are efficiently used over successive generations of farmers. With proper planning, the benefits (income and other) provided by these assets can be maximized. Maximizing these benefits will increase the chances that the farm can help support the retirement of one generation while ensuring that their successors are able to continue to operate the farm. This is complicated somewhat by the fact that farming differs from most businesses in that the residence of the principal owner is often located on the farm itself. In fact, a greater percentage of farmers live on-farm in Tennessee (81.3 percent) than the national average (76.8 percent).[6] One more reason to consider a full-scale succession plan!

Need more convincing? The most common causes of the failures in transitioning family-owned businesses are (1) not having a plan, (2) taxes and/or (3) family discord, all issues that a good family business succession plan can help iron out. Certainly, to do this efficiently, smoothly and in fairness to all parties requires comprehensive planning rather than just a will.

Typical Goals of Farm Succession Planning

Successful farm succession planning is ultimately defined by the achievement of goals that were set forth in the planning process. This manual is designed to assist in defining goals and identifying ways to achieve them. Once the goals are identified, they can be included in each component of your farm succession plan: business, retirement, estate, land, and/or transition – each of which is discussed in detail in the chapters that follow.

Common farm succession planning goals include:

- Maximize net worth of the estate
- Distributing assets in accordance with wishes, including treating all children fairly
- Eliminating, or at least minimizing, cost, delay and public disclosure associated with probate
- Providing for care of minor children and/or other dependents
- Planning for owners' illness or incapacity
- Determining future land use for the long term
- Maintaining quality of life for current owner(s) after succession
- Sustaining profitability during and after the succession period
- Developing a stepwise managerial transition process

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Chapter 2: The Family Discussion

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Why Is Communication So Important?

Succession planning contains two parts – economic and social decision-making[1]. Most families focus on the legal and economic issues but fail to give the attention needed to the social issues. Losing sight of social or family-level concerns surrounding the distribution of assets, transfer of a business and preservation of a legacy will create more problems than the succession planning process can solve. Communication is the cornerstone to any successful succession plan. When communication is lacking, there is no way of knowing whether the plan is addressing or poised to accomplish what the family really wants or needs.

Other reasons to start a family conversation include:

- Discussing your plan with your family and heirs can relieve stress for you and for them. Both generations may be wondering and worrying about what will happen to the family farm and they likely share some of the same concerns. Talking about and discussing the issues may relieve some of the burden created by not sharing and might even soothe the anxiety both generations could be feeling.
- Keeping the estate or succession plan a secret can lead to family conflict. After a death, a serious illness or injury is not the time family members want to be surprised. Explaining your decisions to family members can reduce the potential for conflict and misunderstandings, especially if assets are divided unevenly. Seemingly loving, friendly siblings can change their demeanor when parents are no longer there and assets are being divided.
- Talking about your wishes for the farm and farm family can help you clarify your own wants and needs. If you wish your parents could work less and relax more, maybe you need to take over more of the farm operations and management. If you never want to see the farm developed for non-farm purposes, then maybe you need to learn more about a conservation easement.

Why is it so Difficult?

If communication and discussion are so important to the success of not only the succession plan, but also the family and family business, why don't more people do it? Perhaps, it is because people often avoid situations that have the potential to be uncomfortable or result in change. What is overlooked then is the indisputable fact that at some point in the future, the current owner and manager will no longer be able to run the farm operation. As the saying goes, "The only two things you can count on in life are death and taxes." However, many current owner/managers decide to bury their head in the sand and ignore the obvious. Thus, in many cases, the "succession" occurs without the "planning" and the farm business has less of a chance for survival.

Let's face it, sitting down and talking about succession planning is about control, wanting more of it or not wanting to let it go. It is about admitting to oneself and to each other that there will be an end to the way we know things. It is about making difficult decisions that may or may not hurt someone else's feelings. Those are weighty topics in and of themselves. Then add all the laws, regulations, tax issues and the ever-present "elephant in the room" – financial issues – and it is understandable why families don't find it popular dinner conversation. Succession planning can be tedious, complicated and emotionally draining at times, but difficult decisions need to be made.

In fact, there is even a term for all the reasons why people don't start the succession planning process: "the succession conspiracy." Coined by Ivan Landsberg, the 'conspiracy' is a function of four elements: the owner (often the founder or direct descendant of the founder), family, employees (family and non-family) and the environment in which the succession planning is going to be conducted. Table 2.1 [2] on the following page illustrates elements of the "Succession Conspiracy."

Each of the elements 'conspires' against the successful fulfillment of succession planning, oftentimes before it gets started. For the founder, even mentioning succession may be painful, because it may conjure uncomfortable feelings about the inevitable (our deaths) and serves as a signal that the timeline for running the farm is finite. With farming often being an integral part of an owner's self-identity, succession of the farm means a loss of power and a tangible labor of love that makes the owners 'who they are.' By thinking of succession in these terms – fear and loss – the owner will be very reluctant to hand over the reins and may hold feelings toward the successor that are not constructive. This could adversely affect the owner's personal legacy, as well as the legacy of the farm.

Table 2.1: Elements of the "Succession Conspiracy"

Founder	Family	Employees	Environment
• Fear of death • Reluctance to let go of power and control • Personal loss of identity • Fear of losing work activity • Feelings of jealousy and rivalry toward successor	• Founder's spouse's reluctance to let go of role in firm • Customs against discussing family's future beyond lifetime of parents • Standards against favoring siblings • Fear of parental death	• Reluctance to let go of personal relationship with founder • Fears of differentiating among key managers • Reluctance to establish formal controls • Fear of change	• Founder's colleagues and friends continue to work • Dependence of clients on founder • Cultural values that discourage succession planning

In much the same way, the other elements – family, employees and environment – can conspire against succession planning. For example, familial values and customs may override the desire for the farm business to be passed on to the next generation. Driven by the fear of change or the potentially uncomfortable position of having been designated over someone else, the employee may not want to put succession, or even planning for it, into motion. Lastly, the environment in which the planning is to take place may not be conducive to succession planning.

Wow, sounds like fun! As compared to the alternative, you bet it is. The alternative to discussing and deciding what is best for the family could be someone outside of the family deciding what happens. Or worse, it could be having a poorly designed succession plan that ends up destroying a family, ending a business and ending a legacy. The legal and emotional costs that could come from not discussing or not having a plan more than likely will outweigh any costs or discomfort incurred in investing in a well-designed succession plan.

How Can I Make It Less Difficult?

Each family is unique. Some families may find it easy to talk about their feelings, wishes and plans, while others may find it a very difficult and intimidating task. Below is a list of items that could help lessen the difficulty of discussing and planning the future of the farm operation.

- *Plan early.* This really needs to be bolded, underlined and in all caps. **PLAN EARLY**! Some families don't plan or begin to think about planning until a crisis has occurred. This is not the best time to be making difficult decisions. At that point, it may be too late and the decisions may be out of your hands.

- *Start with the positive*. It might help not to start the conversation with, "Mom, Dad, what is going to happen to the farm business when you die?" A better starting point might be, "Mom, Dad, I would like to start taking more responsibility on the farm. How could I help?"

- *Focus on the items you agree on.* If you both want the farm to stay in the family, then start there and begin the conversation. The more controversial topics will begin to trickle into the conversation. At least you have begun building the lines of communication.

- *Maintain open communication and LISTEN*. Allow those involved to feel comfortable sharing their feelings and listen to them when they do so.

- *Make no assumptions about the feelings or plans of others*. People are full of surprises, even those you may have known your entire life. Assuming is guessing and guessing means there is room for error. Like the teacher always says, "If you are not sure, ask."

- "*R-E-S-P-E-C-T, find out what it means to me."* Respect each other. You don't have to agree on everything, and more than likely you won't, but being respectful of others involved will grease the wheels of communication and create a smoother process.

How Do We Start the Conversation?

Listed below are several conversation starters that can help you or another family member begin the planning process. However, before starting the conversation, the

first step is to decide who will be or should be involved in the discussion. This is not as easy as it sounds. Ask yourself: Who will be affected by this plan, both directly and indirectly? And remember, being inclusive at the onset of the process will likely mitigate issues that would otherwise creep up if particular family members are left out of the conversation. In other words, while it might be easier to leave some people out of the process, it is better to include them now than to have them insert themselves later on, after feeling left out or excluded. Keep in mind that these individuals may have not even set foot on the farm in years! Though some individuals may only be a factor in one element of the succession plan (e.g., estate planning), they should be included or kept abreast during the entire process. In any case, making the entire process inclusive and transparent helps to create the necessary “buy-in” prior to implementation of the succession plan.

Once the potential participants are identified, then it is matter of deciding the best way to approach each one and encourage them to open up. No matter how you start the discussion, once it is initiated, it should be easier to discuss the family's situation, concerns and goals.

Possible ways to start the conversation include:

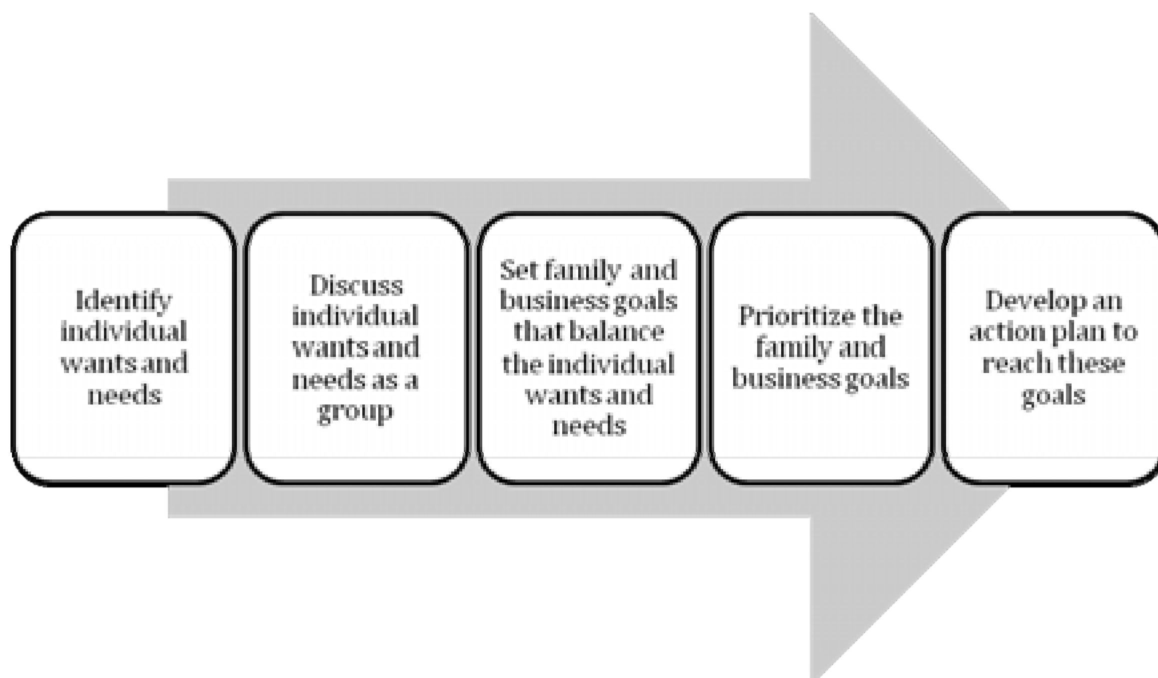
- Using this publication as a conversation piece. Share what you learn at the workshop or in this manual with other family members and encourage them to read the material.
- Stimulating conversation by reading books, magazine articles and other publications related to succession planning. From farm magazines and newspapers to Extension publications and other reputable sources, bringing up something you heard or read is a natural and unintimidating way to lead into the discussion.
- Using someone else's story to get started. It's tragic, but the death of a neighbor, friend or relative may lead a family to realize that succession planning is not a subject to be overlooked.
- Sharing your preferences and plans in the event of your own serious illness or death, in the hopes that this will spur another family member to open up.
- Having a family meeting. The initiator must realize and be prepared for some family members’ willing participation, some members’ refusal and others seeking more information before they decide to participate. A family meeting could be as easy as a 20-minute conversation after everyone has come together for dinner. It doesn’t have to be formal with a planned agenda – it just has to get everyone in the same room for a conversation.

What Do You Want the Plan to Accomplish?

Wants, Needs and Goals

As you will see, farm succession planning – if done well – follows distinct steps. Though they may be intertwined across different elements of the succession plan, these steps are often sequential, requiring the completion of one step prior to beginning another (Figure 2.1).

Figure 2.1. Steps in the Family Discussion for Goal Setting



After initiating the dialog, all family members should think about and identify their individual wants and needs for themselves, the farm operation and their family. Worksheets 2.1 and 2.2, located in the appendix, are provided to help you and your family in this process. It is important to keep in mind the difference between a 'want' and a 'need.' A 'need' meets a basic requirement to live and survive. In the realm of succession planning, ensuring that all planning elements are legal and that income post-retirement will provide a manageable quality of life for the older generation are common examples. A 'want' can be thought of as something that the individual, family or business can "live without." While needs typically supersede wants, a succession plan should strive towards meeting needs and balancing wants.

What needs to be discussed?

(excerpt from *"Farm Transfers in Wisconsin: A Guide for Wisconsin Farmers"* a publication from the Wisconsin Farm Center[3])

Transfer of the family farm includes major decisions involving career choices, lifestyle changes, retirement considerations and assumption of debt. Before any decisions are made about financial or legal agreements, each family should give careful thought to their own wants and needs. Each family should spend time thinking and talking about what is important to them. Then, the two families need to get together for open discussion about how each family's needs can be met. If the family farm transfer is an intergenerational transfer, from mom and dad to one or more of their children, there should be several family meetings with both generations coming together to discuss issues of concern.

What is critical, however, is that the two generations get together to talk openly and honestly about their wants, needs and goals for the future.

Once the individual assessment of wants and needs is completed, all those involved should get together and respectfully discuss everybody's specific wants and needs as a group. Obviously, this should be done before any legal and financial decisions are made, because if the financial and legal arrangements do not meet the needs of the parties involved, there may be increased family discord and the farm business may suffer. Sharing collectively as a group serves to strengthen the trust and relationship among family members, which will in turn strengthen the succession plan.

The discussion could be conducted over a series of family meetings where each person takes turns explaining what he or she hopes to accomplish with a succession plan. If it is difficult for some to openly talk about their wants and needs, then ask that they write their thoughts down and someone else can share them. No matter how you get together and how you discuss the wants and needs of all, it is important for everyone to be actively involved and for the information generated to be archived (e.g., meeting minutes or notes) for future reference.

Setting Goals

Once all parties involved have identified their individual wants and needs, it is important to come together as a group to set goals that will balance the needs and wants of all involved. For example, the successor(s) may want to take over the farm tomorrow, but the current owners may want to be involved indefinitely into the future. Somehow, these differing wants must be addressed and an agreeable goal defined. The objective is to reach a decision (among the current owners and the successors) about goals for the business and the family.

Most goals can be divided into two categories: business and family. Business goals are those that relate solely

to the business and its operations. In contrast, the family goals relate more to the wants and needs of the family's desired legacy or the family members' desired lifestyle. Defining the business and family goals of the succession plan will allow a family to convey to professionals, such as attorneys and financial planners, exactly what they want their plan to accomplish.

Business Goals

Business goals may be as simple as production goals, enterprise goals or business growth goals. Business goals could also include the financial objectives desired, such as a reliable and regular cash flow. This is perhaps the most important influence in deciding what *mus*t be done as opposed to what is *wanted*. Cash flow needs to increase as the family grows. When two generations are farming together, the division of cash and assets will be a significant aspect in the relationship between the generations. Other possible business goals include minimizing taxes during and after transfer, and/or minimizing settlement costs such as legal fees.

Example:

- **Individual needs**
  - *Older generation*: We need to have enough money to support us through retirement.
  - *Younger generation*: We need to have enough money to support our family's needs now and in the future.

- **Business Goal**
  - Increase cash flow and profitability of farming operation

Family Goals

Family goals could be to continue farming or preserve the farm with a conservation easement. Other family goals could relate to family relationships, such as the goal to maintain a close family relationship and remain good friends during the entire succession process. They could be as simple as the goal to have grandchildren not living on the farm visit and grow up with the ability to experience the "farm life."

Example:

- **Individual wants**
  - *Older generation:* “I want my daughter to take over the farming operation.”
  - *Younger generation:* “I want to continue farming on the family farm.”

- **Family goal**
  - Transition ownership of the farm to the daughter over a five-year period.

Reaching a Decision

The ultimate goal – a successful farm business – is the culmination of individual, family and business goals being set and put into motion. These goals are not set in a vacuum; there is often a significant amount of overlap and interplay during their development and implementation. As the family defines goals, it is important to keep in mind that some goals may receive priority over others. This is an important part of how the goals will be implemented, as it may be only feasible to achieve one goal before addressing the next goal. That said, some of the goals will be accomplished concurrently. Arriving at the point of goal and priority setting means that decisions should have been made. Hofstrand (2007) outlines the four methods that family businesses can use to arrive at decisions regarding establishing and setting priorities[4]:

- **Autocratic:** Use for routine decisions where others don’t feel a need to be involved.

The autocratic methodology involves a single decision maker (typically the principal operator) while all others are forced to abide by the decisions made. This method often takes very little time – an advantage when a quick decision needs to be made – but does not allow for input from other family members. This can be a source of resentment.

- **Democratic**: Use for large group decision-making, or where consensus or collaborative decision-making is inappropriate or fails.

At first glance, this may appear to the best choice for all decisions. Our nation was founded on the principles of democracy, after all. However, when making family business decisions, the ‘majority rules’ aspect of the democratic method can be a source of resentment for the minority. An advantage of the democratic method is its application when there are a large number of family members involved in the decision and/or the issue is contentious and other methods have proven ineffective.

- **Consensus:** Use for decisions where facts can be used to outline pros and cons.

By definition, consensus involves reaching a general agreement among decision makers – here farm family members – and does not imply that everyone is 100 percent "on-board" with all of the decisions that have been made. However, for consensus to work, everyone must eventually support the final decision. Therefore, the hallmark of a long-lasting consensus is solidarity. In other words, although there may be disagreements involving some of the details, the group is willing to move forward together in unity of purpose.

- **Collaborative:** Use for making major business decisions that require the support of everyone involved to be successful.

Related to consensus building, the collaborative method brings all ideas to the table and relies on all family members to explore fully all options prior to making a decision. While consensus building results in a decision being made with at least 'buy-in' from all parties, collaborative decision-making seeks to find a solution that is agreed upon, by all parties, essentially without reservation. In the short term, the collaborative process is the most time-consuming, as considerations are fleshed out during each meeting, but the decisions made through the process are most likely to stand the test of time.

No matter the decision method used, moving forward involves putting together a feasible action plan and providing a means of dealing with any conflict.

How Will We Accomplish What We Want?

The Action Plan

After goals and priorities have been defined and decisions made, it is important to develop the action plan for reaching the desired goals. Goals can be broken down further into objectives (smaller steps toward reaching the goal with a shorter time frame of completion) and individual action steps that lead toward achieving objectives and ultimately the goal. Worksheet 2.3, located in the appendix, gives you a template for mapping out your action plan.

The action plan to attain goals and objectives should include:

1. Setting goals, objectives and action steps
2. Setting a target date for reaching goals (medium/long-term) and objectives (short/medium-term)
3. Setting deadlines for completing action steps (short-term),

4. Specifying who is responsible for each goal, objective and action step
5. Identifying resources necessary to achieve goals
6. Evaluating progress toward meeting goals
7. Reinitiate the goal-setting process as needed

Example:

Using the two previous examples where the older and younger generation defined a family goal and a business goal, this example will walk through the action plan for reaching those goals.

Background on operation:

- Father/daughter dairy operation
- 150 acres
- 100 cows
- 10 acres of sweet corn
- 5 tractors
- 4 barns

Business Goal: Transition ownership of the farm to daughter over a five-year period.

Objective	Action Steps	Deadlines	Person (s) Responsible
Transfer of management of 10 acres of sweet corn to daughter	Develop a marketing plan	March 2010	Daughter
	Determine production practices (fertilizer, seed)	March 2010	Daughter

Family Goal: Provide desired quality of life for both generations.

Objective	Action Steps	Deadlines	Person (s) Responsible
Increase cash flow and profitability of farming operation for distribution as outlined in the transition plan.	Meet with UT Extension area farm specialists to go over finances	November 2009	Father/Daughter
	Investigate other farm enterprises to diversify operation	January 2010	Father/Daughter

Balancing the Concerns of Many

The wants and needs of all parties involved will not always be the same. More than likely they will differ by generation and relationship to the owner and business. The 65-year-old retiring farmer will have different wants and needs from the 25-year-old beginning farmer. A non-farming family member will have different wants and needs from the farming family member. These differing wants and needs are due to the different concerns, values and lifestyles of the involved parties. Following are some things to consider when discussing the wants and needs of everyone involved. It is important that everyone try to understand the other's point of view and understand that there may be certain issues that are not easy to bring up or to resolve.

Things to Consider: Current Owner/ Older Generation

- **Not just a business.** The current owner/older generation will often have concerns about entrusting "their" business and the legacy "they" have built and managed to someone else. This is even more apparent in farm businesses where the farm is much more than just a business. The farm could be the home, income, retirement and family heritage of the older generation, making it difficult to let go.

- **Not ready to walk away.** The owner may want the farm to stay in the family and continue as an operating farm while staying physically or financially involved in the operations. However, it is important for the older generation to realize at some point that they have to let go of the reins and allow the next generation to take control.

- **Retirement.** Older generation family members could have concerns about whether the business assets will be able to generate sufficient income to support

them throughout their retirement. They need to ask themselves, “Do we want a large cash payment upfront or a steady income from the farm through a contractual agreement with the next generation?” The older generation will need to think through their financial needs and plan for covering costs such as insurance, health care and other day-to-day living expenses.

- **Where do we live?** Do you want to continue to live on the farm or move off-farm? Is there space available for the future generation to build a home? Living arrangements will need to be discussed, as the older generation may need or choose to continue their residence on the farm.

- **Fairness.** Some concerns of the older generation could include their desire that the succession plan should treat all of their children fairly and equitably. This issue is of particular prominence in families with children who are not directly involved with the family business. As the saying goes, “Equal is not always fair and fair is not always equal.”

Things to Consider: Future Owner/ Younger Generation

- **To farm or not farm?** The first question a young farmer should ask himself or herself before getting involved is, “Do I really want to farm?” Farmers are entrepreneurs and, as with all entrepreneurs, there can be many rewards but also many challenges. Make sure *you* want to farm and that you and your family will be willing to work though any challenges that may arise.

- **Economic viability**. Am I going to be able to make enough money to support my family? The economic viability of the farm operation is of utmost concern to the younger generation. And if the older generation wants to remain involved or still retain income from the business, the question changes to, “Would the family business be able to support both generations at the same time?” These are questions that need to be thought through and may involve working on the current and future business plan of the farming operation. It could be that significant changes are needed to ensure future economic viability, such as adding more acreage or buying more or newer equipment. Young farmers need to think not only in the short-term but also in the long-term, as family needs can change as the family grows and children get older.

- **Will I be a partner or a hired hand?** Future owners may have concerns about whether they would be treated as partners or as hired labor after the transition. What amount of managerial freedom would they have? Would they be able to implement new ideas or make significant changes to the operation? When will

they begin to gain equity in the operation? Discussion of roles in future managerial and production decisions should be discussed to deal with the concerns.

- **How much do we owe?** Farming can be a debt-heavy occupation. Capital and operating costs can be high and a bit daunting for young farmers. There may be concerns about the stress of high debt loads necessary to maintain or expand the current operation, as well as the possibility of having to buy out senior and non-business family members. If the older generation wants to slowly transition out of farming, they may consider selling or transferring assets over a period of time instead of upfront. This may help young farmers ease their way into ownership and manage the debt more efficiently. It is important for the younger generation to be aware of the debt and to decide whether or not they want to or are capable of taking on the debt load.

- **Can I have the lifestyle I want?** How much time do we get away from the farm operation? How much time do we need to spend with our family? Young farmers may want a different lifestyle than the older generation, including time for family vacations, home improvements and other fun activities. Can they have this lifestyle without guilt and criticism from the older generation?

A word of caution

A warning to those young farmers who have returned to the farm and are working day after day, putting their money, sweat, blood and tears into the operation under the naïve assumption that, "of course" the farm will be theirs. This is an assumption no one can afford to make. No matter how hard it is to start the conversation, find a way and get the assumption transformed into fact by having it formally stipulated, in writing, in the succession plan.

Things to Consider: Off-farm Family Members

- **What about what I think?** Many non-farm heirs may feel left out or excluded. Just because they are not there on the farm every day does not mean they do not care. They are a part of the family and their thoughts and concerns should be listened to and addressed.

- **If you get the farm, will it stay a farm?** Off-farm family members may have concerns about protecting the farm from development or protecting the family legacy but have none about the day-to-day activities of the farming operation. If this is the case, then their concerns can be addressed by agreeing to support the

farming family members as they strive to keep the land agricultural or preserving green space by using a tool such as a conservation easement. However, off-farm heirs may want assurance that agreeing to and supporting the decision to give the farm and farm assets to the farming heir means that the farming heir won't turn around and sell the assets. This is double-edged sword, though, because there may be a point where the farm will have to be sold due to economic situations. The farming heir can't be tied to farming forever just because the farm was given to him or her. These issues should be addressed and discussed.

- **I just want to sell.** It may be that the off-farm family member is more interested in the financial proceeds of selling the property, while the farming family members do not want to sell, but actively farm the land. Whether driven by the potential for personal financial gain or simply a lack of concern about protecting the farm and family legacy, selling the farm will likely be a source of tension. This is one of the most common conflicts amongst siblings of farming parents. All too often there may be only one child who wants to continue farming, while the others have moved off the farm and into different occupations. This issue can be complicated and full of emotion and should be addressed by both generations honestly and respectfully. Certainly arrangements can be made, but they are not sustainable if they leave the farm business extremely vulnerable or the remaining farm family's situation economically infeasible.
- **If I don't get the farm assets, what do I get?** If non-farming family members do not want the farm, then possibly there are other assets including investments or non-farming property that could be given to them in an estate plan. For example, if the family decides to place a conservation easement on the property, the proceeds from the sale of the easement could go to the non-farming sibling and the land could go to the farming sibling. The land and operational equipment can be given to the farmer and the liquid assets to the non-farmer.

Equal vs. Fair

Some farming parents feel the property should be divided equally, while others are more concerned that the property or estate be divided fairly. Fair may mean equal or it may mean a division of property that reflects the time or money that each child has invested in the farming operation, knowing that some may have invested considerably more than others. The question that has to be asked, "Do you want to transfer assets or a business?" If you are interested in just passing down assets, then divide equally and move on; however, if you are interested in passing down a business, then effort must be made to keep the assets together that will make the business successful and profitable. A farm divided could be a farm lost.

When There Is Conflict

Despite all of the best efforts of each family member, the farm succession process is not without potential for conflict.

A transparent understanding of each family member's needs, values, perceptions, goals, feelings and interests will provide a solid foundation from which to move forward. Thoughtfully integrating these individual goals with family and business goals is a positive step. Using appropriate decision making methods and conducting constructive family meetings can help create 'ownership' of the decisions made and avoid the alienation that is sometimes extremely difficult to avoid.

Unfortunately, succession planning does not always go as smoothly as the family would prefer. This potential for conflict is often the reason why primary operators put off the inevitable. However, not wanting to "stir the pot" puts the farm and the family in a position of even greater conflict when the primary operator dies unexpectedly. This conflict and lack of planning can

FAIRNESS
(excerpt from University of Wyoming's *Passing it On: An Estate Planning Resource Guide for Wyoming's Farmers and Ranchers* by Lucy Pauley, Alan Schroeder, Cole Ehmke and Carolyn Paseneaux[5])

It's tempting to think, "They're my kids, and they should all get equal shares." With that attitude, passing on the ag operation as a viable entity will require jumping some tremendous hurdles. First, the business operator probably isn't going to be able to afford to buy out the off-farm heirs – principal and interest payments may be overwhelming, and the size of the operation may be insufficient to support a family. Second, joint ownership of the business by people who will certainly have different goals will make decision making difficult. Don't force siblings with different goals to work together. Finally, dividing the business assets equally does not reward the child who worked on the operation. This is not being fair.

The senior generation needs to define what is fair, then share that reasoning with the others involved.

have a significant effect on the legacy of the farm.

Usually the biggest hurdle to succession planning is the actual initiation of the process. By killing the notion before the planning process ever leaves the gate, farm businesses are put in a precarious position – one where succession may not even be possible after the owner has passed. Other times, the family decides with good intentions to develop a succession plan. A family meeting, or series of meetings, is called and all of the appropriate people are around the table. Despite the inclusivity and transparency of the process, some family members may choose to be disruptive to prevent or terminate the proceedings. This is when conflict truly rears its head and the decision-making methods being employed may not succeed in overcoming the impasse. While conflict isn't necessarily bad – it can motivate useful debate and ensure a full examination of the issues – it can devolve into less than constructive behavior. At this point, a mediator may be necessary or the family can attempt to use some of the conflict resolution techniques listed below. If the situation is getting exceedingly difficult and tempers are flaring to the point of irrevocable damage to the family and its business, a professional should be sought immediately to mediate a solution.

If conflict does arise, Dr. Dudley Weeks[6] has developed a framework that seeks to develop partnership from conflict through effective conflict resolution. He outlines eight steps to follow:

1. **Create an effective atmosphere**: Just as communication provides the foundation upon which succession planning takes place, conflict resolution needs to take place in an atmosphere that cultivates resolution rather than poisoning the waters of discourse. Approaching the conflict by fostering positive interactions at a mutually appropriate time and place makes resolution more likely to occur.
2. **Clarify perceptions**: Family members who are in conflict during the succession process often think they know what is motivating the other party. This perception is often wrong or misinformed and rooted in issues that are as much a part of the individual's own perceptions as they are of the other person. To avoid having perceptions ruining what should be a constructive process, both parties need to be honest about what the root causes of the conflict are and focus on a resolution that respects the entire family relationship and does not dwell on 'winning.'
3. **Focus on individual and shared needs:** As was mentioned earlier, beginning the communication process involves indentifying individual

wants and needs. As needs commonly trump wants, the parties involved need to focus on what their needs are and which needs are shared (an indicator is that these needs are family needs and should take priority). By focusing on shared/family needs, the parties can realistically consider the root cause of the conflict and steer resolution towards addressing these needs, in addition to those of a more individual nature.

4. **Build shared positive power:** During conflict, family members usually attempt to wield power against one another to gain advantage over the other in an effort to 'win.' By focusing on shared needs, the parties can use 'positive' power towards a constructive resolution.
5. **Look to the future, then learn from the past:** Certainly, successful operation of the farm is as much a function of the land as the personalities who run the farm. Family farms are often rooted in history and tradition. The current status of the farm is of course a culmination of all the decisions that have been made prior to today. While families in conflict can learn from their history, the probability of resolution will be higher if the family focuses on the present and future and doesn't dwell on the past in an unconstructive way.
6. **Generate options:** A constructive resolution process should focus on generating options rather than entrenchment of both parties through their demands. This requires that each person is willing to 'think outside the box' and generate options that may not resemble his or her original position but will address the shared needs of the family.
7. **Develop "doables" – stepping-stones to action:** Oftentimes, the ultimate solution (goal) is made up of several action steps. These steps or "doables" may be less contentious than the final solution, but can move the family forward in a positive and constructive way. Breaking down the issues into component parts and identifying steps with a high probability of accomplishment requires participation of all members and meets shared family needs. The march toward resolution has begun.
8. **Make mutual-benefit agreements:** Honestly discussing shared needs and identifying "doables" should lead family members toward an agreement that will ultimately lead to resolution of the conflict. (This can be thought of as a mutually beneficial goal that will be incorporated into the succession plan.) Once agreement is reached, it

needs to be 'solidified.' Review the agreement to be sure everyone understands it completely. Use whatever means is agreeable to ensure that the agreement remains in some kind of reviewable form (family meeting minutes, informal contract, checklist, etc.) and ultimately incorporated, as agreed upon, in the succession plan.

Having gone through the process in a positive and constructive way will likely lead to further application when the need arises. As with all elements of the succession plan, conflict resolution is a process that requires implementation, evaluation and adjustment as time goes on.

Seeking Professional Services

After the initial discussion has happened and you have set goals and priorities, then developed an action plan, it is time to put together your professional succession planning team. These experts will help you implement your succession plan and could include a realtor, financial planner, attorney, accountant, farm management specialist, forester, or other professionals. You may have already identified and used professionals during the goal setting or planning process, but choosing the professionals who will constitute the team is an important decision for you. Chapter 6 will help you indentify criteria on which to select an attorney. Tips are provided to prepare you for the first visit and the relationship between you and your attorney.

You Can't Quit Talking

Running a farm is one of those occupations where it is often said, "I love it because it is something different every day." It may be the weather, disease, crop prices, input costs or technological change, but whatever the case, agriculture never stands still and each season is different from the last. In the same way, your succession plan must be able to adjust to the times and accommodate unanticipated changes.

This means that a succession plan should be treated as a 'living document' that is revisited by the farm family on a regular basis. When there are changes in the family such as divorce, remarriage, or death (in either the younger or older generation), this should trigger the discussion and re-examination of the succession plan if it had been completed previously. The reality is that family members have "standing" in a family business whether they are new to the family or have been associated for a long time. By initiating an ongoing process for evaluation and updating, your succession plan will be flexible enough to handle most situations and robust enough that it will not change in its entirety every time an action step is abandoned or an objective is altered. This can be accomplished by:

- Always keeping the communication channels open
- Faithfully conducting constructive family meetings
- Performing all of the necessary record keeping in a timely and accurate manner
- Maintaining contact with all members of the succession team, including paid professionals
- Honestly evaluating progress towards achieving goals and completing the action plan

Pitfalls to Avoid

A list of pitfalls to avoid from *"What Good Is It if We Don't Get Along? or Planning for Family Harmony"* by Verlyn De Wit.[7]

- Giving children grossly unequal shares of the estate. While children may appear to get along very well, things tend to change when property is going to be distributed.
- Punishing financially successful children by decreasing their inheritance. Many children are driven to success simply to please their parents. Decreasing the inherited share of a successful child is a crushing blow to the over-achiever. Here is an ideal example of a situation where discovering expectations could lead to a much more desirable distribution plan. What if, for example, the financially successful heir who is CEO of a giant company would prefer that his or her share go to the sibling who had spent his or her life teaching elementary school students?
- Forcing children to own property together after your death, leaving the heirs to decide how to split the property.
- Requiring the off-farm heir to take his or her inheritance in the business as a long-term loan to the on-farm heir. Children don't do well in debtor/creditor relationships.
- Failing to communicate your plan to your children. Explaining the plan to all the children is especially important when children are treated differently to arrive at what the senior generation believes to be a fair and equitable resolution. It is best to avoid surprises.
- Planning late. A study sponsored by National Life of Vermont examined 749 family businesses that failed within four years of being transferred to the second generation. It found that more than 97 percent of the inheritors blamed the founders for being negligent in preparing for the transition, or for having an inadequate estate plan. Some methods of equalizing inheritance to your children take many years to accomplish. Postponing your planning will reduce your options.

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Chapter 3. Taking Stock of Your Estate

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Preparing a succession plan is important at any age and stage of a business or farming operation. Taking stock of your farm or business inventory and personal information is one of the first steps in developing a succession plan. Accurate and comprehensive records can facilitate this process. Many decisions will revolve around the accurate assessment of an individual's property. These records can also provide a roadmap to greater profitability and productivity if analyzed and used to make management decisions.

Taking stock of an estate includes:

1. Identifying assets and liabilities in the estate.

2. Locating papers and documentation.

3. Establishing a personal net worth.

Complete, accurate records are needed for income tax reporting, obtaining credit, making management decisions and meeting institutional requirements. Taking stock involves compiling a list of your assets and liabilities to assess the overall position and value of your estate. This assessment should be made early in the planning process so that it can facilitate the decisions you need to make. You must have a clear and concise picture of what is included in the estate before you begin developing your succession plan.

All business deals and transactions must be shared and accounted for when putting together this piece of the succession plan. Begin working on your list of assets and liabilities today. This will clarify how you want to dispose of your property as well as assist your advisors on the best methods to use in developing your succession plan. They must have complete information about your estate to be able to predict estate and inheritance taxes and provide advice for your situation.

Steps in the Process

Setting financial goals and determining progress toward reaching them are difficult without knowing the extent and value of the estate. A very effective tool for financial planning is a personal net worth statement or balance sheet. This gives a snapshot of the inventory process and a clear presentation of the information gathered. A net worth statement is a financial balance sheet. It presents a concise summary of your assets

(what you own) minus your liabilities (what you owe) at some point in time. The difference between the two is your net worth.

Preparing a net worth statement will help you get a clearer understanding of the state of your financial resources. To complete a net worth statement, follow three steps to take stock of your estate:

1. Determine what you own and its value
2. Determine what you owe and its value
3. Construct a personal financial balance sheet

Determine What You Own and Its Value

You have an estate if you own anything. Your estate includes real and personal property in which you have a right, title or interest, and all of your assets and liabilities. Your estate includes your obvious personal assets, such as your home and money, and not-so-obvious assets, such as the value of term life insurance.

Start by listing all your assets – what you own. Personal assets include liquid or cash assets, such as cash on hand and money in checking and savings accounts. Invested assets include certificates of deposit, mutual funds and marketable securities like stocks and bonds. Include assets in taxable accounts as well as those in tax-deferred accounts such as IRAs and other retirement savings plans, including those provided by your employer. Other assets are your personal property, vehicles, furnishings and home if you own one.

When it comes time to plan an estate, you will need information on:

- the original cost of assets (plus the value of improvements)
- current fair market value
- ownership, names of co-owners (how the property is titled, i.e. jointly with right of survivorship)
- the remaining value of debts
- location of property maps, funds and other important pieces of information.

Values listed for the assets should be both their current market value and what you paid for them. If you were to sell these assets on the open market, what would their value be? Some assets like a home or jewelry may appreciate, but most depreciate or lose value from the original purchase price. Below are tips on how to find values for some assets.

- ***Cash***: Use the most recent statements for checking, savings and money market account balances, and current certificate values.
- ***Government savings bonds***: Call a bank to find out what your bonds are currently worth.
- ***Life insurance policies***: Check your policy or call your agent to determine the cash surrender value and the face value of the policy to be paid at death. Such assessments make a sizeable difference in the value of what you may transfer at any given time.
- ***Stocks, bonds or mutual funds**:* Check a newspaper that publishes the information or read the most recent statement or check with broker.
- ***Residence:*** Use the current value of your house or other real estate – not what you paid for it. Your city or county assessor can tell you the property's full assessed or appraised value.
- ***Automobiles:*** Check a used vehicle guide for the value of your cars and trucks. One example is Kelly's Blue Book (www.kbb.com)
- ***Recreational vehicles:*** To find out the value of your boat, camper, snowmobile or any other recreational vehicle, talk to a dealer who sells used recreational vehicles.
- ***Household property:*** Make a conservative estimate of the value of household items and personal property, recording what you could get if you sold everything today.
- ***Investment accounts:*** List the current value of your pension, IRAs or other retirement plans, using the amount you would receive if you were to cash them in today.
- ***Land:*** Appraisal of the asset (land, improvements, machinery and equipment, water, timber, livestock) is necessary at some point in the planning process.
- Don't forget to add money others may owe you if you realistically expect to collect it.
- Value all of these assets on the same date and put that date on your balance sheet.

Business-related assets you own can be added in a separate section of the net worth statement. For a farm partnership, include only the items you own or owe, not those owned or owed by the partnership. As a part of the business operations, there may be financial statements showing assets, liabilities and net worth. However, this will likely include items that you don't own, and will not have the sort of detailed information required for estate planning. Generally, property that you own jointly with another person with a right of survivorship will automatically pass to the other joint owner upon your death. For example, if you have a joint savings account with a right of

survivorship with your daughter, when you die your daughter receives all the money in that account. Even if your will says to divide everything among your three children, she will automatically get the money in your savings account. It doesn't matter what your will says in this situation. It is very important that you know how you own all of your property and how that property will change hands upon your death. In the case of the bank account, it may be wise for you to be the sole holder with your daughter having a power of attorney to write checks on it.

Determine What You Owe and Its Value

Liabilities are what you owe – usually in the form of outstanding bills and debts. Short-term debt includes current unpaid bills as well as the balance owed on any installment loans, car loans, credit card accounts, loans against life insurance policies and any other secured or unsecured debt that is less than five years in length. Long-term debt includes a home mortgage, home equity loans and any other debt that will take longer than five years to pay.

Worksheets are provided in the appendix of this workbook to assist you in listing your assets and liabilities. Below are tips on how to find values for some common liabilities.

- ***Mortgage:*** The balance of the mortgage loan on your house may be on your monthly statement. If not, ask the lender for the outstanding balance.
- ***Unsecured credit:*** Record the balance due on all credit cards, charge accounts, installment accounts and other loans. Be sure to list the total balance due, not just the monthly payment.
- ***Accounts:*** List any current unpaid bills, including what you owe the dentist, this month's utilities, telephone charges, etc.

Construct a Personal Financial Balance Sheet

After you have compiled both your assets and your liabilities, you are ready to construct a balance sheet. Worksheet 3.1 in the appendix of this workbook will assist you in preparing your balance sheet and net worth statement. A balance sheet consists of current, intermediate and long-term assets and liabilities. ***Current assets*** are those expected to be sold or used within the next year. ***Intermediate*** and ***long-term assets*** are those with a longer life expectancy such as equipment, land and timber. ***Current liabilities*** are those that are expected to be paid back within the next month or year. ***Intermediate*** and ***long-term liabilities*** have a term longer than one year. However, bear in mind that all intermediate and long-term liabilities still have a current portion that is due each year or each month, which may be interest-only or interest and

principal. Contributed capital and retained earnings are also found on the balance sheet. Your net worth is calculated by subtracting total liabilities from total assets.

Once you have completed your net worth statement, take time to look it over and make sure it is complete. To begin, look at each major liability listed and see if a corresponding item can be found under the asset side. If a corresponding asset cannot be found, you may have forgotten to list something. Or, the asset originally acquired with borrowed money may have already been sold or used up before paying the corresponding liability.

Analyzing Your Net Worth Statement

Your personal net worth statement can tell you many things and can lead to startling insights about your financial condition. For instance, the estate may be much smaller or larger than expected. Your net worth may either be a positive or negative number. Use the information on the net worth statement as the base for financial planning decisions as well as estate transfer decisions. Ask yourself these questions:

- Do you have adequate emergency funds?
- Did you discover any surprises, like excess debt or forgotten assets?
- Is your insurance coverage adequate to cover the value of your property?
- Are your invested assets working for you to increase your net worth?
- How does your debt load compare to your income?
- Are you building financial resources to help you achieve your long-term goals?

A particularly useful calculation based on the net worth statement is the ***estate tax*** (covered in Chapter 5) amount that will be due on your death. The information can be used to create one (or more) hypothetical tax returns. Keep in mind that the amount of the estate tax depends upon the value of the assets you hold in your name at death, how the assets are held, and deductions and credits available. Careful planning often reduces the taxes due.

If the estate is somewhat less than you expected, then in the coming years you may wish to emphasize accumulating assets, or, if you are satisfied with the size of the estate, then you may want to preserve your assets. Estate planning involves the coordination of all your properties (stocks, bonds, cash, real estate, business interests, life insurance, retirement benefits and other assets) into a total program over your lifetime.
Your net worth statement is a record that should be updated on a regular basis and kept with your valuable papers. It should be updated every few years or after some

important life event has occurred, such as after children finish college, retirement, marriage or divorce, the addition of children or grandchildren, a business success or failure, a series or gifts or other important events.

Record Keeping for Improved Decision Making

Record keeping is not exactly the most exciting activity, but the information you can glean from records may answer many questions about your personal and or farm finances as well as provide you with the tools to make informed decisions. Oftentimes, personal and business or farm-related income and expenses are comingled in the same accounts. If this is the case for your operation, please consider separating the accounts.

Worksheet 3.2 in the appendix assesses your record keeping skills for both personal and business items. This quiz can be used to determine how complete your record system is and how prepared you are to begin the succession planning process.

Which Records Should Be Kept?

When determining which records to keep, it is important to determine your reason for keeping them. If you are only keeping records to complete your tax information once a year, you will probably have limited information to make management decisions. The majority of farm operations file taxes using cash accounting. Cash records include farm income and expenses, employee payroll, 1099s, asset sales and purchases. These records should be kept for three to seven years in the event of an IRS audit.

Financial records need to be kept in conjunction with production records. Yield, production practices and unique external factors should be kept so the history can be consulted when questions arise.

Why Should I Keep Records?

Records can be viewed as the health physical of the operation. Poor performance can be quickly identified with comprehensive records. Often, the answer to the problem is just as visible as the problem itself. Records can help determine which area of the operation is the most profitable. They help to measure productivity and financial well-being, as well as to analyze financial position and net worth.

Records are important for many reasons. Records serve as proof of business transactions that occurred during the year. The IRS could ask for proof of income, expense and inventory items reported on tax returns. Records can assist in making decisions concerning business operations by constructing balance sheets, cash flow and

income statements. Government and lending agencies require financial and/or production records to be maintained for a period of time. With increasing environmental regulations, fertilizer and chemical applications must be monitored and recorded.

Records are also needed for completing IRS schedules and other tax purposes. Adequate records are imperative not only for preparing tax documentation, but also in the event of an audit.

Records help you prepare for the unexpected. Farm families are faced with unfortunate circumstances at times and past information can prove beneficial. Disaster, disability and death totally change the framework of and relationships within a family.

To effectively manage your operation, you must be measuring inputs and outputs. This information is a communication tool and can be used to plan ahead and analyze the business. Financial statements, both historical and projected, must be developed with accurate records to have an accurate vision of the business. Many lending institutions require financial statements and those statements must be positive to receive additional funding. Hopefully, your financial statement is growing and increasing over time. Records can also assist in the development of a spending plan, break-even analysis, marketing plan, enterprise analysis, investment analysis and risk assessment.

How Often Should I Analyze or Use My Records?

Records can answer questions at any point in the operation or at any point in the year. You can analyze the current year as well as multiple years. When analyzing these records, include business, production and personal information as often either farm or non-farm income is subsidizing the other. Taking a historical look at your operation can give you an idea of relative strengths and weaknesses and may suggest ways the operation can be improved. Looking at the operation under current conditions may provide the information to tackle problems before they get out of hand.

Records offer cold, hard facts about the business. These facts make it possible to compare your operation with industry benchmarks. You have insights into strengths and weaknesses and are better equipped to identify problems. When those problems are identified and addressed, maximizing returns to the resources you own becomes an attainable goal. Complete records can also provide you with information regarding the feasibility of a new venture.

Record Keeping vs. Record Analysis

The primary difference in record keeping and record analysis is the ability to use records in making informed decisions. A business may keep records to maintain information for tax purposes; it will then be categorized and filed in the appropriate location. This can be accomplished using a variety of methods, from a basic hand record-keeping system to an elaborate computerized system. With record analysis, the records that have been filed are further evaluated to make decisions. Establishing and using an effective record-keeping system allows for making informed decisions based on actual or projected performance.

Selecting a Record Keeping System

You may be wondering what methods are available to keep records or assist you with keeping records. Two general methods are the hand system and a computer system. With the hand system, there is low initial out-of-pocket expense for pen, paper and a calculator. Depending on the type of computer system and then the desired software program, a computer system can have a substantial initial out-of-pocket expense. The hand system is easy to implement by writing down the information to be tracked, while a computer may require a significant amount of study, from learning how to use the computer itself to studying the specific functions of a software program. The hand system can be time-consuming, from designing the layout of the records to making calculations by hand. Once you understand the use of a computer program, it will calculate information rapidly. Making calculations by hand allows more opportunities to make mistakes. Once you have mastered entering information into a computer program, and have entered the information accurately, the computer is generally accurate at analyzing the data. With a hand system, you may be limited in the extent of analysis you can perform without expending a lot of time and effort to design a financial tracking system. The major benefit of a computer system is, of course, the power of analysis.

Think about your operation and the type of information you would like to track and report. These decisions will guide you in choosing the system for your operation. You may desire features that are easy to use, flexible, able to adapt with a changing operation and inexpensive. You may also want to track both farm or business and family records. There are products that range from simple and relatively few entries to comprehensive packages providing many added features that you may or may not use.

As a business man or woman, you should ask yourself these three basic questions:

- Where am I financially?
- Where do I want to be?
- How can I best get there?

Chart your course with a mission statement and goals and make the changes necessary to reach the results you want.

Centralizing & Securing Your Important Documents

Securing your financial documents and important papers in a central location is a necessary component of successful record keeping. Keeping your records in a specified place is more than a matter of organization. Legal and safety factors must be considered as well. Some records and papers can be kept in a home file for easy access and use, while others should be kept in a safe-deposit box or in a fireproof, waterproof and burglar-proof home safe, or left with an attorney. A good rule to follow is to keep the item at home unless it is a legal document that is difficult to replace or duplicate. In that case, it should be kept in a safe-deposit box or with your attorney.

Grab It and Go!

You are told that a natural disaster is going to destroy your home or business in 10 minutes. You have 5 minutes to get anything from your home or business that you might need, and then 5 minutes to travel to safety. What do you take with you?

If the scenario to the right of the page were to occur, you might feel very prepared. However, if you are like many people, your information can be found in several locations around your home or business, and you don't have a clear idea of what you would need to grab in an emergency situation.

When considering where to store documents, there are many available options. These include a home or business filing system, a home or business safe, safe deposit boxes or with family members and attorneys. Depending on the information to be stored, each of these solutions may be useful, and are discussed in the following section.

Home or Business Filing System

Households are a mini-business, since the functions of planning, purchasing and record keeping are the same as they are for any other business, large or small. It is helpful to follow a plan for tracking information as well as storing important papers in a specified location. This will ease tensions when emergency situations arise and can help preserve peace of mind among family members. The focus of a home or business filing system should be to create a space for your needs. For some, a cardboard drawer, metal box or

filing cabinet may suffice, while others may work better having a "business corner" in some room of the home. The important thing to remember is to have an inviting space that you will be willing to work in several times each month.

A filing system must be set up to meet your needs. If you are new to record keeping or need a new system, create any files you may need in advance and add to them as you gather information. This will assist you in filing the information rather than adding it to a pile of papers. Once you develop a system for storing your documents, be consistent with the location and method used.

Home or Business Safes

When choosing a safe to be used in your home or business, consider the features of the safe and the items to be stored, as well as the location where the safe will be used. Options for smaller spaces include chest-style, file safes, locking file cabinets and wall-mount safes. In-floor safes may also be an option for storing smaller items. If you need to store several documents, personal possessions and large items, you might consider a floor safe.

Security features, fire endurance and water endurance are also things to consider when choosing the right safe for your needs. Safes lock in a variety of ways. Some have multiple locking features, which may include a key, a combination, an electronic keypad or a fingerprint identification system. Fire protection time can range from 30 minutes to two hours and can withstand temperatures ranging from 1550 to 1850 degrees F. Many safes also offer water-resistance features. Some safes also endure drop tests, which may be tested from 15 to 30 feet.

Safe-Deposit Box, Family Members or Close Friends, Attorney

A safe deposit box can serve as an additional place away from your home or business to store those hard-to-replace documents. A family member or close friend should have a copy of your important documents in the event of an emergency or disaster. This also makes certain that someone else knows your wishes. An attorney should have a copy of those legal documents that are difficult to replace or duplicate.

Guide to Storing Important Information

Once you are ready to begin filing your important documents, you must plan and evaluate your chosen storage method. Any item that is a permanent or semi-permanent record should be kept in a safe-deposit box or a fireproof, waterproof, burglar-proof safe. File important information promptly, or throw items away if they are no longer

needed. Due to the danger of identity theft, consider shredding any document containing personal information, including name, address, Social Security number or debit/credit card numbers.

Permanent and Semi-Permanent Records

Permanent and semi-permanent records can be categorized into four areas: family, property, financial and legal. The following tables, adapted from Montana State University, reference each area and include the items to keep, the reason for keeping those items and the length of time to keep them. Some of the records may be stored in a home file, while others may need to be housed in a more secure location. You have many important papers relating to personal records, property ownership, insurance, finances and other business affairs. Worksheets are located in the appendix to help you inventory your important papers, locate papers when needed, direct others in an emergency and evaluate your family business affairs. Fill in the worksheets and keep them at home. Review them at least once a year, and bring them up to date when a significant change occurs. You may wish to prepare a copy for a relative or close friend for use in an emergency.

Table 3.1 **Family Records**

Item to Keep	Reason for Keeping	Length of Time to Keep
Baptismal and confirmation records	Proof of church membership	Indefinitely
Insurance policies: Automobile, personal or business liability, life, health, disability, homeowners or renters; List of policy numbers, name of each insured, beneficiary, company agent with phone number	Reference for kinds and amounts of coverage; provides record of payments, premiums and location of policy; provides record of claims	Until collected or expires; until all claims settled
Passport	Identification required for international travel	Retain expired passport to satisfy application requirements for a new one, then discard/destroy

Item to Keep	Reason for Keeping	Length of Time to Keep
Wills (copy)	Reference; essential for settlement of estate	Keep original indefinitely in safe deposit box or with attorney
Education records / diplomas	Proof of attendance and degrees	Indefinitely
Employment records	To determine retirement benefits or if there is a worker's compensation claim	Keep last official announcement of earned benefits; keep record until all worker's compensation claims are settled; keep beyond retirement in case you decide to re-enter the workforce
Licenses to practice (copy)	To verify credentials	Usually displayed; replace with most recent verification; keep copy in a safe place
Family advisers: Names, addresses, phone numbers, email addresses	Ready reference when needed (medical, legal, etc.) arises	Update when changes are made
Medical history: Immunizations, operations, illnesses, medications, etc.	Reference	Indefinitely on all family members; update and review often
Funeral plan documents	Reference	Indefinitely; update as needed
Subscriptions and buying clubs: Titles with order & renewal dates; membership details	Reference	Until subscription expires; handle complaints or cancellations
Organizational memberships	Reference	Until membership is cancelled

Item to Keep	Reason for Keeping	Length of Time to Keep
Keys (labeled) to safe-deposit box, vehicles, house, home safe, safe combination	Access as needed	Until property is sold or safe-deposit box is relinquished

Table 3.2 **Property Records**

Item to Keep	Reason for Keeping	Length of Time to Keep
Abstract for real estate	To prove clear title	Until property is sold
Automobile title and bill of sale	Proof of ownership	Until vehicle is sold
Burial lot deed (note number of plots)	Proof of ownership	Indefinitely
Deeds and mortgages: Title policy; property insurance policy; mortgage; receipts for payments on mortgage; day, month and year your acquire or sell property; gross sale price; depreciation; legal fees and expense of sale	For income tax and estate tax purposes; keep records of improvements to compute capital gains or losses	Until property is sold to prove your home's adjusted basis
Household inventory: Appraisals, photos/videos of valuables; record item, cost, date of purchase	For insurance claims to establish values; net worth statements; pictures are helpful when making claims	Keep list up to date as you dispose of or add items; make a copy for safe-deposit box
Property easements	Proof of use rights	Until property is sold
Appliances and other manuals	For reference on use and care/repair	Until sold or discarded
Guarantees and warranties	Proof of date of purchase; to determine service and parts guaranteed	Until no longer valid

Item to Keep	Reason for Keeping	Length of Time to Keep
Pets/livestock: Pedigree, health and license records	Identification	Until animal is sold or dies

Table 3.3 **Financial Records**

Item to Keep	Reason for Keeping	Length of Time to Keep
Contracts, notes, debts: Promissory notes, mortgages, liens, installment contracts	Evidence of collectible or payable debts; status for estate settlement	Until estate is settled
Investment certificates: Stocks, bonds, mutual funds, CDs, real estate	Proof of purchase; statement of earnings and transactions as reference information	After redemption amount received and taxes are settled on gain or loss; keep initial and current investment quarterly statements
Account books: Goals, spending plan, record of income and expenditures	For reference and comparison; used to determine net worth and make changes in income and spending patterns	Personal choice; shows profit or loss over multiple years
Checking accounts: Account numbers, location, addresses, phone numbers, bank statements/canceled checks	Reference for completed transactions (deposits and withdrawals)	Minimum of at least six years of checks
Credit and debit cards: Name, address, phone number of company, card numbers (photo copy front and back)	Purchase of items on credit or from checking account	If card is not in current use, cancel by writing to company; if lost or stolen, notify company immediately by phone
Housing/business records: Improvement receipts, lease/rental agreement copies, utility deposit receipts, mortgage payments, property tax records	Compute capital gains/losses; income tax basis	Keep records until property is sold and after as required by law

Item to Keep	Reason for Keeping	Length of Time to Keep
Receipts and receipted bills	Proof of payment/value	Keep credit card receipts until bill is paid; keep larger item receipts while items are in your possession
Income tax returns: Federal returns with substantiating records	Verification of taxes filed/paid	Three years minimum for possible IRS audit; unlimited if you file a fraudulent return
Retirement records: Employee pensions, annuities, IRAs, etc.	For reference; proof of employer/employee contributions; payments and benefits received or payable	Until fund is exhausted

Table 3.4 **Legal Records**

Item to Keep	Reason for Keeping	Length of Time to Keep
Birth certificates (certified copy or original)	Proof of birth	Indefinitely
Death certificates	Proof of death for Social Security benefits and estate settlement	Until benefits are secured and estate settled; note cause of death for family health history
Marriage records	Proof of marriage to collect insurance, Social Security or retirement benefits	Until all claims are settled, benefits are received and estate is settled
Divorce decree/settlement	To clear legal requirements for remarriage	Indefinitely
Adoption papers	To prove ages for school, drivers license, marriage license, voter registration	Indefinitely
Military service	To qualify for retirement, insurance, medical, education, burial and other benefits	Indefinitely
Citizenship and naturalization papers	To obtain certain types of jobs, passport; prove eligibility to vote	Indefinitely

Item to Keep	Reason for Keeping	Length of Time to Keep
Living will (original with additional copies made)	Reference specifying your end-of-life care; instructions to your doctor and other health care providers; instructions for close family members	Keep a list of where copies are distributed to be able to provide most recent copy if changes are made
Will and/or trust (copies)	Unsigned copy for home reference	Update copy if will or trust is changed, keep until updated
Durable power of attorney for financial decisions: Specify the extent of power delegated to one or more persons	Gives others the power to make business decisions when you are no longer able to make decisions on your own	Keep until updated, not valid after death
Durable power of attorney for health care	Gives others the power to make health care decisions when you are no longer able to make decisions on your own	Keep until updated, not valid after death
Personal representative and guardian and conservator appointments	For official notification of agent to settle estate and provide for care of children and their finances under legal age	Until official duties are completed and court order closes
Social Security card	Needed to apply for benefits; identification number needed on many types of applications and records	Indefinitely, do not carry in your wallet/purse because your identity could be stolen

Along with storing important documents in your home or business, there is also important information you carry with you in your purse or wallet on a daily basis. Be sure to make a list of these items for your home file in the event your purse or wallet is stolen. These items may include credit and/or electronic banking cards, driver’s license, auto insurance card, donor card, health insurance card, preferred doctor and organization membership cards. In case of emergency, you should also carry your medical information: blood type, allergies, diseases (such as diabetes, heart disease, epilepsy, etc.).

Once you create your home or business filing system, the work doesn’t stop there. Information should be reviewed and updated at least once a year. When special events

such as a marriage, birth, home purchase or death occur, records should be revised at that point.

You must be the one to make the final decisions on which records to keep and where to store them. You may choose to be more or less detailed, depending on your needs, wants or stage in life. The most important factor is to start somewhere and keep track of your information.

Items of Sentimental Value

When making plans for your estate, items such as land, the house and bank accounts rise to the top of the list. But what is often forgotten is who will receive grandma's recipe book, old family photos or grandpa's antique pocket knife. These items tend to cause immense tension among family members and may be some of the most important "small items" of the estate. An estate plan should not overlook these items, nor should an inventory of assets.

"The fundamental problem is that personal possessions often can't be distributed equally to more than one heir," explains Marlene Stum of the University of Minnesota. "Money can be split in thirds, but a painting, for example, cannot. People have far more emotional attachment to personal items than to money, which makes the division process potentially traumatic."

Sentimental assets should be listed separately from financial assets due to the nature of their special characteristics. Construct an inventory listing of personal possessions along with their special meaning and potential recipients of the items. However, the personal asset should be listed on the personal balance sheet if the asset has significant financial value. Worksheet 3.4 is available in the appendix for you to begin an inventory of your items of sentimental value.

The steps to developing a written plan are:

- Keep your checkbook recorded and balanced
- Write out the details
- Allocate every dollar
- Commit to the plan

Family Living

An important piece of information affecting the farming operation as well as the family is accurately tracking family living expenses. Although developing a written budget doesn't sound like much fun, proper planning today can lead you toward a debt-free future. The best written plan comes from good communication and input among all family members and is implemented by all family members as well.

Worksheets 3.5, 3.6 and 3.7 in the appendix provide you with a chart to track family living expenses, lump sum payments and special expenses that occur throughout the year, respectively. Family living expenses include many different categories, such as monthly costs of groceries, utilities, mortgage payments and transportation (which occur each month). Other expenses, including insurance, taxes and tuition, occur annually or semi-annually. For these infrequent expenditures, you may find it helpful to use lump-sum payment planning and save a small amount each month rather than taking a large sum out of a single month's income. For example, if your family's health insurance cost is $1,200 per year, you may opt to save $100 a month so that when the expense is due, you already have the money set aside. The "Reminder of Special Expenses Worksheet" can assist you in tracking those annual and semi-annual expenses or special events to remind you when they are due. Make sure you are keeping accurate records of your family living expenses, as they are most often only estimated, but may be significantly underestimated.

Signs of Identity Theft

- Bills do not arrive as expected
- Unexpected credit cards or account statements
- Denials of credit for no apparent reason
- Calls or letters about purchases you did not make

Once It Happens

- Place a fraud alert on your credit report
- Close accounts
- File a police report
- Report theft to Federal Trade Commission

Identity Theft

Another important reason to track your personal information is the risk of someone stealing your identity. You should take the appropriate steps to prevent becoming a victim of identity theft. Thieves have developed complex skills in retrieving your personal data, despite your efforts to manage your information. They may steal your mail (including bank and credit card statements), purse or wallet, or personal information through e-mail or phone by posing as a legitimate company and asking you questions about your account.

Once an identity thief has your personal information, he or she can use it in a variety of ways. Thieves may call your credit card issuer to change the billing address on your credit card account or open new credit card accounts in your name. When they use the credit cards and don't pay the bill, the delinquent accounts are reported on your credit report. Thieves may

open a bank account in your name and write bad checks on that account or buy a vehicle and take out an auto loan in your name. Most frightening may be having a driver's license issued in your name with a thief's photo on it.

While there is no definite way to keep identity theft from happening to you, there are steps you can take to minimize your risk.

1. Shred any outdated information containing your name, address, birth date or Social Security number. Also destroy old debit/credit cards.
2. Detach your personal information from credit card offers and destroy them.
3. Protect your Social Security number. Don't carry your Social Security card in your wallet or write your Social Security number on a check.
4. Review your credit report at least once a year. An amendment to the federal Fair Credit Reporting Act requires each of the three nationwide consumer reporting companies to provide you with a free copy of your credit reports, at your request, every 12 months. Visit www.annualcreditreport.com to order your free annual report. Each consumer reporting company – Equifax, Experian, and TransUnion – is required to give you a free copy of your credit report each year, if you ask for it. You can call toll-free 1-877-322-8228, or complete the annual credit report request form.

Some companies offer types of insurance claiming to give you protection against the costs associated with resolving an identity theft case. As with any product or service, make sure you know what you are getting before you purchase.

For assistance with establishing a record keeping system, developing your balance sheet or deciding which pieces of information to keep, contact your county UT Extension office for assistance through the MANAGE Program. The MANAGE Program was designed specifically to help Tennessee farm families carefully evaluate their individual situation and assist them in improving their quality of life.

The MANAGE program helps families analyze their total farming business so they can make informed decisions regarding their future. Staff trained in farm and financial management help families:

- review their current financial situation
- capitalize on strengths and reduce weaknesses in the farm business
- develop individualized farm and financial plans
- explore alternatives both on and off the farm

- evaluate capital investment opportunities including land and/or machinery purchases
- analyze likely consequences of changing the scope of enterprises
- determine appropriate production practices

Although the MANAGE program will not remove the uncertainty of the future, it can provide you with a clear understanding of your current financial situation and help you evaluate your alternatives for the future. Making informed decisions today may be the best way to prepare for tomorrow's opportunities. The educational program is offered at no cost to participating farm families in all 95 Tennessee counties. Families are not formally enrolled into the program and all information remains confidential.

References:

This section was written in part with information adopted directly from "Passing it On: An Estate Planning Resource Guide for Wyoming's Farmers and Ranchers" Authors: Lucy Pauley, Alan Schroeder, Cole Ehmke and Carolyn Paseneaux, Wyoming Agriculture & Natural Resource Mediation Program in conjunction with the University of Wyoming Cooperative Extension Service, June 2006.

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Chapter 4: Business and Organizational Structure

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Introduction

An important part of succession planning is selecting an organizational structure for the farm business. While choosing an organizational structure is important for reasons having nothing to do with succession planning, this chapter will focus on the importance of this choice to successful succession planning.

A first step in discussing this choice is to consider exactly what comprises the organizational structure of a farm or family business. We can think of organizational structure as including the following three components:

- **Management Structure.** The management structure determines how decisions are made and responsibilities allocated among the individuals in the business. A clearly defined management structure lets all involved know not only what their roles are and what is expected of them but also how decisions concerning the farm will be made and who will make them. While a hierarchical, top-down management structure (where decision-making authority is retained at the top) remains popular, there is evidence that successful family businesses often rely on shared decision making. While older or more experienced managers often have a difficult time accommodating the ideas of younger, less experienced operators, this difficulty is often magnified when the younger, less experienced operators are also the offspring of the older, more experienced operators.
- **Financial Structure.** The financial structure of the business defines how ongoing business operations are financed and how the income from the business is distributed among those who have contributed, leased or loaned physical, human or financial capital to the business. Two aspects of a business' financial structure are worthy of particular attention within the context of a succession plan – the opportunity for investment and the sharing of business income. The transition from the current owners – who have often accumulated significant business assets over a lifetime of work – and new owners – who are often just starting out and thus may have limited assets and borrowing capacity – will often require a very different financial structure. At one extreme, the new owners may borrow extensively (either from lending institutions or the current

owners) to purchase assets, and at the other extreme the new owners may purchase assets gradually by plowing profits back into the business and building equity over time. Given that the accumulation of business assets by the current owners often occurs at the expense of investment in more traditional retirement accounts, a division of farm income that supports both the old and new owners and allows the new owners to invest in the business can be difficult to achieve.

- **Legal Structure.** The legal structure defines the legal relationships between and among the current and future owners, as well as the relationships between the current and future owners and third parties, such as lenders, vendors and buyers. These legal relationships are defined by the (i) legal entity under which the current owners operate the business; (ii) nature of transfer of ownership, management and control from the current to the future owners; and (iii) legal entity under which the future owners operate the business. This chapter includes an overview of the different legal entities from which a farm or family business is likely to choose, along with a discussion of the factors that should be considered when choosing a particular legal entity. The ways in which ownership, management and control can be transferred from current to future owners are discussed both in this chapter and in Chapter 5: Estate Planning Tools.

Succession planning thus implies that, in choosing an organizational structure, business owners should consider not only how management and control will be structured, but also how they will be transferred from one generation or owner to the next. In many instances, this transfer may be gradual, with the existing owner relinquishing management and control to the new owner over time. While a gradual transfer may benefit both parties, the temporary sharing of management and control can be difficult. In fact, the success of multi-generational businesses can depend quite crucially upon the ability of family members and others to work together effectively. Worksheet 4.1, The Multi-Generational and Joint Business Operation Quiz, in the appendix can help you evaluate the strengths and weaknesses of the individuals who are going to be involved in the management and operation of the business. These difficulties can also be affected by the choice of organizational structure. In addition, the way in which the business is transferred from one generation or owner to another is likely to be affected by financial or credit constraints. These constraints may also affect the choice of organizational structure.

The remainder of this chapter discusses particular aspects of these three components of organizational structure and how they relate to succession planning in more detail. However, the focus of the chapter is on the second component – legal structure – in

part, because it involves a number of technical terms and concepts with which many people may not be familiar. Much of what follows in this chapter assumes that the succession plan does not include the termination of the farm or family business. That said, the general concepts and principles discussed in this chapter are generally relevant for those instances in which the result of the succession planning process is that the land will no longer be used for farming or the business will be sold.

Following this introduction, the chapter moves to a brief overview of the three general ways in which the ownership, management and control of the farm or family business may be transferred from one generation or owner to another. This overview is followed by a more detailed focus on the use of legal agreements and entities in this process, including a discussion of critical problem areas and of the legal arrangements for transferring ownership, management and control of the farm business. The chapter then turns to a discussion of legal entities, discussing both the factors to be considered in choosing a particular entity and how the different legal entities perform. Finally, the chapter ends with a few concluding thoughts. Readers who are interested in more information on any of these topics are encouraged to consult those resources listed in the Additional Resources section of this workbook.

General Forms of Succession Plans

The different ways in which the ownership, management and control of the farm business are transferred from one party to another can be grouped into three broad categories, described as follows:

- **Spin-off.** In a spin-off arrangement, a new farming enterprise is spun-off or created that is separate and independent from the existing enterprise. For these arrangements, the structure of the existing operation typically changes very little. The parties often share labor and machinery and, over time, the new enterprise builds equity and takes over an increasing part of the operation of the business. These arrangements are based on an implicit or explicit (oral or written) agreement as to how the business will be transferred over time. Thus, the relationship between the parties is contractual in nature and often fairly short-lived. The success of spin-off arrangements depends upon the parties having similar expectations as to the transfer of the business; explicit agreements between the parties put in writing to reduce conflict and the timely development of the new enterprise into a sufficiently profitable operation.
- **Landlord/Tenant**. In a landlord/tenant arrangement, the current owner of the business retains ownership of some or all of the farm or business assets and leases these assets to the new owner. This type of arrangement is often used to

provide the current owners with income in their retirement years while the new owner builds the financial or borrowing capacity needed to purchase the assets. The success of these types of arrangements depends upon the current owners being able to accept both a reduced role in farm or business management and a reduced income from farm or business operations.

- **Superfirm**. In a "superfirm" arrangement, one or more entities are created that survive the transfer of the farm or family business. These arrangements require the use of a separate legal entity, such as a partnership, corporation or limited liability company, and imply at least a period of co-ownership of the farm or family business. Transfer of management and ownership of the entity can occur gradually over time through sales, gifts and bequests at death. An advantage of these types of arrangements is the flexibility they provide. For example, these arrangements may make it easier for parents to include off-farm heirs in the ownership (if not the management) of the farm than other arrangements. On the other hand, these arrangements may be more complex and more costly to create and maintain.

Each of these types of arrangements has advantages and disadvantages. The type most appropriate for any particular set of circumstances depends upon a number of factors, including:

- The nature of the farm or family business;
- The current and future profitability of the farm or family business;
- The value of the assets associated with the farm or family business;
- The desires and preferences of both the current and future owners of the farm or family business;
- The financial position and income needs of the current owners; and
- The financial position, knowledge and experience of the future owners.

Regardless of which type of succession plan is used, the legal nuts and bolts of the plan will typically consist of one or more contractual arrangements between the parties (unless transfer of management, ownership and control occurs exclusively at the death of the current owners) and one or more legal entities under which the farm business is operated. The following sections focus on these contractual arrangements and legal entities.

Contractual Agreements

A number of different contractual arrangements may be used during the transition from one farm owner to another. These agreements typically fit into one or more of the following four broad categories: employment, sale, lease and financing. It is possible for a single agreement to span more than one of these categories, as might be the case with a lease/purchase agreement, for example. In general, it is preferable that these agreements be written and properly executed by both parties to avoid disagreements over the terms of the arrangement. In addition to avoiding faulty or incomplete recollection of the specifics of the agreement, putting the agreement in writing may promote a more complete specification of the relationship and a more careful consideration of the implications of the agreement by the parties.

Employment Agreements

A common relationship between a retiring and a beginning farmer or family business owner is that of employer-employee. This relationship can allow the new owner to accumulate experience and assets while maintaining considerable flexibility for the parties as they move forward. Legally, there are essentially two different types of employment – at will and contract. At will employees can resign or be terminated by the employer at any time, without notice or justification. Contract employees are hired pursuant to an oral or written contract that provides the terms of the employment. Employment contracts typically set forth the conditions under which the employee can be terminated, as well as the process for doing so, and may also specify notice or other requirements for resignation by the employee. Thus, at will employment retains maximum flexibility with a minimum of commitment, while an employment contract requires greater commitment but can provide the parties with some assurance of certainty regarding the nature and continuation of the employment.

Employees can be compensated in a number of different ways. The most basic form of compensation is the payment of wages, typically stated in terms of an hourly, weekly or monthly amount and paid weekly, biweekly or monthly. The wage rate paid depends upon the skill level of the employee and the demands of the employment. Sometimes, a portion of the wages is paid in the form of commodities instead of cash. Employers may also offer incentives that involve payment of pre-specified amounts in exchange for the achievement of pre-specified performance standards or goals. For an incentive plan to work, the reward offered must be in line with the value the employer obtains from the achievement of the goal or standard and the effort required by the employee. Incentive payments differ from bonus payments in that bonuses are not designed to provide increased compensation for a specific achievement, and thus are not typically contingent upon anything other than continued employment. Thus, bonuses are

typically designed to reward the employee for tenure in the job or to boost employee morale. Income sharing can be used to provide employees with a more general incentive. For example, under a wage and income-sharing plan, the employee is paid a combination of wages and a share of firm income or profit. This provides the employee an incentive to contribute positively toward the enterprise while maintaining the employer-employee relationship instead of creating a partnership between the parties. Finally, employers often offer employees a variety of fringe benefits, such as meals, housing, health insurance, disability insurance and contributions to a retirement plan. Fringe benefits are often not taxable to the employee, making their after-tax value much higher than equivalent wage or other monetary payments.

Leases

A lease for real property (land and what is attached to or growing upon it) is a contractual arrangement by which the landowner (landlord) grants another party (tenant) an estate in land for a fixed period of time in exchange for the payment of rent. In Tennessee, real property leases for more than a year must be in writing to be enforceable. The payment of rent in leases for agricultural property can be structured in a number of different ways, depending upon how the risks and rewards associated with yield and price variability are to be allocated between the landlord and tenant.

- **Fixed Cash Lease**. Under a fixed cash lease, the tenant pays rent that is either a fixed amount per acre or a fixed amount for the entire farm. The tenant bears all of the production and price risk.
- **Flexible Cash Lease.** Under a flexible cash lease, the amount of rent paid by the tenant fluctuates with production conditions (i.e., yield) and/or crop or livestock prices. Landlord and tenant share production and/or price risk.
- **Crop Share Lease.** Under a crop share lease, the landlord shares in the expenses of growing the crops and receives a share of the crops or a share of the revenue generated by the sale of the crops as rent for the premises. Landlord and tenant share in price and production risks.
- **Livestock Share Lease.** Under a livestock share lease, the landlord shares in the expenses of raising the livestock and receives a share of the livestock or a share of the revenue generated by the sale of the livestock as rent for the premises. Landlord and tenant share in price and production risks.

Each of these broad categories includes a wide range of possible arrangements. In addition, there are a number of other important provisions that should be included in a lease and many important factors to consider before negotiating and entering into a lease – too many, in fact, to be adequately covered in this workbook. Fortunately, there

are a number of publications and form lease agreements available to those who are interested in learning more about leases of agricultural lands. References to these publications and form lease agreements are provided in the Additional Resources section of this workbook.

The parties might also choose to lease personal property (essentially, any property that is not real property) such as farm machinery, equipment or livestock. Like leases for real property, personal property leases for a term longer than one year must be in writing to be enforceable in Tennessee. Also like real property leases, more detailed information on personal property leases can be found in the resources listed in the Additional Resources section.

Sales Contracts

Contracts for the sale of real property must also be in writing to be enforceable in Tennessee. Luckily, written form contracts for the sale of real property are readily available from real estate agents and other sources and it is recommended to have an attorney or real estate agent review the contract. However, any contract for the sale of real property should contain, at a minimum, the following:

- Names of the buyer(s) and seller(s);
- Type of ownership interest to be passed from the seller to the buyer, the quality of title and the type of deed;
- An adequate description of the property to be transferred;
- Selling price and time of payment (buyers often try to include a contingency that allows them to cancel the contract if acceptable financing cannot be obtained);
- A description of how real property taxes for the year of the sale are to be apportioned between buyer and seller (for farms, property tax liability is often apportioned by crop year);
- A provision indicating which party bears the risk of loss from fire or other casualty;
- A detailed list of any personal property to be included in the sale; and
- Division of closing costs which will vary depending on financing.

Contracts for the sale of personal property will include many of the same provisions as contracts for the sale of real property. More information on agreements for the sale of

personal property can be found in the resources listed in the Additional Resources section.

Financing Agreements

The transfer of the business or assets of the farm or family business from the current to new owners is often financed through loans. In these instances, the new owners typically borrow from either a bank or other lending institution or the current owners (or, often, some combination of the three). Thus, this section provides a brief overview of some of the legal principles and documents that are critical to financing arrangements where either real or personal property is used as collateral to secure the repayment of the loan.

The one element common to all loans is a promise or I.O.U. by the borrower to pay the lender an amount or amounts of money or other items of value at some specified time in the future. When written, this promise is known as a promissory note. The function of a promissory note is to evidence the debt owed by the borrower to the lender. If this debt is unsecured by any real or personal property, then the **promissory note** is all that is needed. However, if the borrower pledges property as collateral to secure the debt, then one or more additional agreements or documents are required. If the property pledged to secure the debt is personal property, then a security agreement is executed by both parties. The security agreement grants the lender a security interest in the collateral, or the right to take and potentially sell the collateral if the borrower defaults on the promissory note or security agreement.

While the security agreement establishes the rights between the lender and borrower relative to the collateral, the filing of a financing statement is sometimes required for the lender to establish rights to the collateral relative to others. The financing statement is a brief document describing the collateral and providing the names and addresses of the borrower and lender (you will often hear financing statements referred to as a UCC-1, which is the name of the form). If the property pledged to secure the loan is real property, then the borrower signs a mortgage or deed of trust granting the lender a security interest in the real property. Mortgages or deeds of trust are recorded in the county land records, while financing statements are filed with the Tennessee Secretary of State, the county, or both, depending upon the nature of the personal property used to secure the debt.

Important Considerations in Choosing a Legal Entity

Each type of business form or entity has advantages and disadvantages. Thus, no single entity is generally superior to the other entities, and choosing a particular legal entity involves making tradeoffs. The choice of a particular entity should depend upon how

the entity performs on a number of different factors. These factors include the following:

- Management and Control. What are the implications of the business form for the way in which the business is managed and controlled? Some entities allow the business to be run by a single individual, while other entities allow or require that other owners have a say in the management and control of the business.
- Owner Liability. Does the form of legal entity limit the personal liability of business owners for business debts and obligations to the amount of the owners' investment in the business? Or, are the owners personally liable for all of the debts and obligations of the business?
- Tax Treatment. How is the business entity taxed? Some entities are subject to "double taxation" in that the entity is taxed on the profits it earns, while its owners must also pay taxes on the share of these profits that are distributed to them. Other entities are "pass-through entities" in that the entity itself does not pay taxes on its profits. Instead the tax obligation for these profits "passes through" to the owners.
- Transferability of Ownership Interests. How easy is it for business owners to transfer their interest in the business? In addition to being relevant for succession planning, the transferability of ownership interests can also determine how easy it is to raise additional financial capital for the business. Easy transferability makes it easier to attract investors and raise capital by selling ownership interests in the business. However, farm and family business owners may be reluctant to have easy transferability of ownership interests, as they may lose control over who else can become an owner and potentially have a say in the management and operation of the business.
- Continuity of the Business Entity. What happens to the business entity if an owner dies or otherwise withdraws from the entity? Does it continue in existence or must a new entity be formed for the business to continue? The answer varies from one entity to another.
- Start-up Costs and Burden. How extensive are the start-up costs? Some entities have little or no start-up costs, while others involve formal filings with the Secretary of State, along with the payment of filing fees and fees for professional services associated with the creation of the entity.
- Administrative Costs and Burden. How costly and time-consuming is it to comply with the requirements for operating the business entity? Some entities entail formal requirements such as annual meetings and fees in order for the business to continue

to qualify as a particular type of entity. Failure to comply with these requirements can, among other things, lead to a dissolution of the legal entity.

The relative importance of each of these factors will vary from one set of circumstances to another. For example, the limitation of owner liability may be a very important concern if a corn maze is being considered, while the start-up and administrative costs may be very important for a small operation. The next section provides an overview of the different types of legal entities appropriate for a farm or family business and considers them in light of the factors discussed above. In addition, Table 4.1 on page 80 provides a comparison of the entities in terms of these different factors.

Business Insurance

Like the choice of legal entity, business owners can manage their exposure to risks associated with the operation of a business through the purchase of insurance. Insurance coverage is a standard cost of doing business. Sometimes, insurance coverage for a small business may be included as part of a personal policy or homeowner's policy. However, adequate coverage may require a separate commercial policy specifically for the business. Insurance companies offer a variety of different types of insurance coverage for businesses, including:

- **Product Liability Coverage** – protects you if your product causes injury to a consumer;
- **Auto Liability and "Non-owned" Auto Liability Insurance** – protects the business in the event of an accident involving an automobile that is used to support the business;
- **General Liability Coverage** – provides coverage for legal defense and financial compensation and is designed to protect the business from claims filed by third parties;
- **Property Insurance** – protects the business in the event of physical damage or loss from such incidents as fire & theft;
- **Medical Payments Insurance** – protects the business in the event someone is injured;
- **Worker's Compensation** – protects the business if employees are hurt on the job;
- **Business Interruption Insurance or Earnings Insurance** – compensates the business for lost income if the business has to vacate due to a disaster that causes a total or partial suspension of business operations;
- **Disability Income Protection** – a form of health insurance in case a business owner or employee becomes disabled;
- **Business Life Insurance** – provides funds for the transition of the business to a new owner in the event of death of the business owner; and
- **Vandalism & Malicious Mischief Coverage** – Protects the business in the event of vandalism and related crimes.

All insurance policies and business records should be kept in a safe location, and more than one person should know where the policies and records are stored. However, having insurance can provide a false sense of security, so it is important not only to have coverage but to have the right coverage. Business owners should read and understand the fine print in all policies and periodically reevaluate their insurance needs.

(Adapted from: Holland, Rob, 1998. Business Insurance Considerations. Agricultural Development Center, University of Tennessee Extension. Available online at: http://cpa.utk.edu/pdffiles/adc14.pdf.)

Legal Entities

Sole Proprietorship

A sole proprietorship is a form of business organization that makes no legal distinction between the business and the individual owner; they are, in fact, one and the same. Thus, a sole proprietorship is owned by a single individual (often referred to as the sole proprietor) who has full control of the business and is solely responsible for all of the debts and obligations of the business. Any employees are hired by the owner and any contracts entered into are entered into personally by the owner. As a result, the business owner enjoys no limitation of liability and is just as liable for debts and obligations related to the business as the owner is for his or her personal debts or obligations. However, a sole proprietorship can operate under a trade or business name that is different from the sole proprietor's name, which is often described with the phrase "doing business as" as in, John Smith, doing business as Pleasant Valley Farms.

> Before using a trade or business name, the owner should make sure that it has not been reserved or registered by anyone else, by conducting a search through the Tennessee Department of State (http://www.tennesseeanytime.org/sosname/). More information on the registration or reservation of business names in Tennessee can be found at: http://www.state.tn.us/sos/forms/busname.pdf.

Because a sole proprietorship is not a separate legal entity, no agreements or filings are necessary to operate a business as a sole proprietorship (although a business license or permit may be required, depending upon the location and nature of the business). In fact, if a business is operated without taking the steps necessary to create another business form, it is a sole proprietorship by default. Similarly, with a sole proprietorship there is no requirement to keep business and personal assets separate or maintain separate accounts. Thus, a sole proprietorship is the simplest and easiest form of business to start, which probably helps to explain why sole proprietorships are the most common form of business organization in the U.S. and why most farms and ranches are operated as sole proprietorships.

Any income earned by a sole proprietorship is treated as income earned by the owner, and the owner reports all profits and losses of the business on his or her individual tax return. In addition to being subject to income taxes, the profits from a sole proprietorship are generally also subject to self-employment taxes (contributions to Social Security and Medicare – equivalent to payroll taxes for employees). The income

and expenses of the business are reported on a separate schedule – Schedule F for farms and ranches and Schedule C or C-EZ for most other forms of businesses. More information on the tax treatment of sole proprietorships can be found in the publications listed in the Additional Resources section of this workbook.

The transfer of a business operated as a sole proprietorship is accomplished by transferring the individual assets (and possibly liabilities) associated with the business. While the business form imposes no limitations on the owner's ability to transfer these assets, liens or other encumbrances may limit such transfers. No formal documentation or procedure is required to terminate a sole proprietorship. Finally, a sole proprietorship, by definition, terminates upon the death of the sole proprietor.

General Partnership

A general partnership is a voluntary association of two or more individuals, partnerships, corporations or other associations for the purpose of carrying on, as co-owners, a business for profit. General partnerships are typically formed by either an oral or written agreement between the partners, but they can also be implied from the conduct of the partners. In Tennessee, there are no filing requirements associated with the formation of a general partnership. Thus, general partnerships are the easiest co-owned business entity to create. However, written partnership agreements are recommended to adequately set forth the terms of the partnership. More generally, the discussion, negotiation and preparation of an explicit partnership agreement seem to improve the chances that the partnership will avoid problems and satisfactorily resolve problems that do arise. The benefits of committing a partnership agreement to writing likely increase as the complexity, extent and length of the relationship between the partners increase.

Although partnerships are easy to create, they should not be entered into lightly for a number of different reasons. First, all partners in a general partnership are personally liable for the debts and obligations of the partnership. More specifically, partners in a general partnership are jointly and severally liable for partnership debts and obligations, i.e., each and every partner in a general partnership is liable for all of the debts and obligations of the partnership. Thus, if a partnership were to default on a loan, the lender could conceivably collect the entire amount due from any one of the partners. However, any partner who is made to pay more than his or her share of a partnership obligation can seek compensation from those partners who have not been made to pay their share.

Second, any partner in a general partnership can legally obligate the partnership. Thus, if one partner enters into a contract on behalf of the partnership, all partners may be held liable if the partnership fails to fulfill the terms of the contract, regardless of

whether the other partners approved of, or were even aware of the contract. The extent to which individual partners have the capacity to bind the partnership can be limited by the partnership agreement, but this limitation is not effective if the party with whom the partnership is entering into the contract is not aware of the limitation. Finally, partners owe certain legal duties or obligations to both the partnership and to one another, including, for example, the duty not to deal with the partnership as an adverse party nor enter into competition with the partnership.

Unless specified otherwise in the partnership agreement, partners are presumed to share equally in partnership profits and losses. However, partnerships can share profits and losses in any number of different ways through appropriate provisions in the partnership agreement. A common approach is for profits to be shared in proportion to capital contributions, or the value of the money and/or property contributed by the partners to the partnership.

Absent an agreement to the contrary, each partner has equal rights in the management of the partnership business. So, unless the partnership agreement specifies otherwise, each partner is entitled to one vote regardless of the relative size of the partner's capital contributions or right to partnership profits. However, partners have considerable flexibility to specify different arrangements for the management and control of the partnership in the partnership agreement.

For income tax purposes, a partnership is a pass-through entity that does not itself pay taxes. Instead, profits or losses "pass through" the partnership and are reported on the individual tax returns of the partners in accordance with their share of profits or losses. Partnerships are, however, required to file an informational federal tax return (Form 1065) and provide an accounting of each partner's share of profits or losses (Schedule K-1). More information on the tax treatment of partnerships can be found in the materials listed in the Additional Resources section of this workbook.

A partner can assign his or her interest in the partnership to a third party, who gets the partner's right and obligation to share in profits and losses but not the right to participate in the management of the partnership. In general, the withdrawal, bankruptcy or death of any partner dissolves the partnership. In some instances, the partnership agreement may provide for a continuation of the partnership after such an event, but, in effect, a new partnership is formed among the remaining partners. A partnership agreement can provide for partner's rights to purchase the partnership interest of a deceased or disabled partner's interest.

Thus, partnerships can be a desirable entity for the operation of the farm or family business in a succession plan because they allow for co-ownership of the business but are still simple and relatively inexpensive to form and operate. Partners also have a

great deal of flexibility in how they structure the partnership, but exercising this flexibility typically requires more extensive and complex partnership agreements. On the other hand, general partnerships do not limit the liability of the business owners, as all partners are personally liable for the debts and obligations of the partnership. Also, each general partner, typically, has the ability to legally bind the partnership. Thus, owners should be cautious about entering into general partnerships with individuals who they do not know and trust.

Limited Partnership

A limited partnership is quite similar to a general partnership. However, there are a few key distinctions. All partners in a general partnership are general partners who have a right to participate in the management of the partnership business and who have unlimited personal liability for the partnership's debts and obligations. Limited partnerships, on the other hand, not only have one or more general partners, they also have one or more limited partners. A limited partner invests capital in the partnership but does not have the right to participate in the management of the partnership business and does not have unlimited personal liability for partnership debts and obligations. Instead, the liability of a limited partner is limited to the amount of his or her capital contributions to the limited partnership. Thus, if the limited partnership's debts exceed its assets, a limited partner cannot be compelled to make up the difference, while a general partner can. However, a limited partner who participates in the management of the partnership business (i.e., acts as if he or she is a general and not a limited partner) can lose his or her limited partnership status and become personally liable for partnership debts and obligations.

Also unlike a general partnership, a limited partnership in Tennessee must file a Certificate of Limited Partnership with the Tennessee Department of State and pay a filing fee that is currently (2010) $100. Changes in the limited partnership (change in partner's capital contribution, admission of new partner, withdrawal of a partner, etc.) require the filing of an Amendment to the Certificate of Limited Partnership. In addition to the Certificate of Limited Partnership, the partners in a limited partnership often draft and execute a Limited Partnership Agreement that more fully specifies how the partnership is to be structured and operated. A written agreement is not legally required, but is strongly encouraged.

Finally, Tennessee limited partnerships are required to pay franchise and excise taxes (as are corporations, limited liability companies and business trusts, but not sole proprietorships or general partnerships). The excise tax is equal to 6.5 percent of the net earnings from business done in Tennessee for the tax year. The franchise tax is equal to 0.25 percent of the greater of net worth or the book value of real or tangible

personal property owned or used, with a minimum tax of $100 per year. However, those limited partnerships, limited liability companies and limited liability partnerships for which at least 66.67 percent of their activities are devoted to either farming or holding personal residences where one or more of the entity's partners or members reside, are exempt from franchise and excise taxes. To qualify for this exemption, application must be made with the Tennessee Department of Revenue.

Thus, a limited partnership offers one important advantage over a general partnership – the opportunity for some of the business owners to enjoy limited liability. This property is useful for attracting investors who are not to be involved in the operation of the business. Limited partnerships might also be useful in the succession planning context where there are on-farm heirs who are going to take over the operation of the farm business and off-farm heirs who are to share in the profits of the business but not the management or operation of the business. In this case, the parents and on-farm heirs might serve as general partners, who can be paid for managing the limited partnership, while the off-farm heirs or off-farm parents are limited partners. The tradeoff for this limited liability is that limited partnerships are required to file organizational documents with, and pay filing fees to, the Tennessee Secretary of State. In most other ways, limited partnerships are similar to general partnerships.

Limited Liability Partnership

A limited liability partnership (LLP) is a relatively new type of partnership in which all partners enjoy a reduced form of liability in that they are not normally personally liable for the negligence of another partner. This reduced form of limited liability primarily benefits associations of professionals, such as doctors, lawyers or accountants, to protect each other from being personally liable for malpractice claims against of one of their partners.

Corporation

A corporation is a legal entity separate and distinct from its owners. As a result, corporations can sue or be sued, enter into and enforce contracts, and hold title to and transfer property. In this way, a corporation is different from a partnership, which is a joint relationship between two or more parties and actions by the partnership are, in effect, joint actions of the partners. The formation, operation and dissolution of a corporation are governed by the laws of the state in which the corporation is incorporated. A corporation incorporated in one state can conduct business in other states, although it has to qualify as a foreign corporation by filing papers with those states to do so.

A Tennessee corporation is incorporated or formed by filing a charter with the Tennessee Department of State and paying the $100 filing fee. Corporate charters can either be simple documents that provide only basic information about the corporation or more involved documents that describe how the corporation will be organized and operated. Other steps involved in forming a corporation include:

- Choosing a name for the corporation;
- Electing or appointing the initial board of directors;
- Issuing stock to the corporation's owners or shareholders; and
- Drafting and approving the corporation's by-laws, which will govern the operation of the corporation.

Many of these steps are typically taken by an individual or group of individuals acting as the corporation's incorporator(s). The role of the incorporator(s) is limited to getting the corporation up and running, after which the corporation is governed by a three-tiered management and control structure. Shareholders elect a board of directors who are responsible for making policy decisions concerning the operation of the corporation and for hiring officers to oversee the corporation's day-to-day activities. Corporate officers typically include, at a minimum, a president or chief executive officer, a secretary and a treasurer. Shareholders can also vote to amend the corporate charter and by-laws and approve major decisions, such as the sale of substantially all of the corporate assets; merger with, or acquisition of, another business; and dissolution of the corporation. Shareholder votes operate on the basis of one vote per share of voting stock. Corporate profits are distributed to shareholders through dividends declared by the board of directors.

Corporations range from small closely held corporations with few shareholders to large, publicly held corporations with many shareholders and shares that trade in organized securities markets such as the New York Stock Exchange. For many small, closely held corporations, the shareholders are often involved in the management and operation of the corporation, often serving as incorporators, members of the board of directors and corporate officers.

Corporations can issue two different kinds of stock – common stock and preferred stock – although most corporations only issue common stock. Common stock represents ownership of the residual value of the corporation, or the difference between the corporation's assets and liabilities. Each share of common stock gives its holder the right to one vote in shareholder elections. Preferred stock is given certain preferences or rights over common stock. These preferences typically involve the right to receive a

fixed dividend (as opposed to a dividend determined each year by the board of directors) or a greater right to corporate assets upon the liquidation of the corporation. Preferred stock often has either no or reduced voting rights. The preferences and voting rights of preferred stock must be set forth in the corporate charter.

As a separate entity, corporations are liable for their own debts and obligations and corporate shareholders enjoy limited liability, i.e., their liability is limited to the extent of their investment in the corporation. They are not personally liable for the corporation's debts and other obligations. However, shareholder limited liability can be set aside by a court if the shareholders fail to observe the legal requirements for properly organizing and operating a corporation. These requirements (or "corporate formalities" as they are often called) include: adequately capitalizing or funding the corporation; formally issuing stock to the shareholders; filing an annual report and paying annual fees (currently $20) to the state; holding annual shareholder and board of directors meetings; and maintaining adequate records and accounts for the corporation that are separate and distinct from those of the shareholders.

Corporations exist in perpetuity unless voluntarily terminated by their shareholders or involuntarily terminated in a bankruptcy proceeding. In general, shares of stock in a corporation are freely transferrable by the shareholders and subsequent owners of the shares have all of the rights that prior shareholders had. The ease with which corporate shares can be transferred gives corporations an advantage in raising capital through the sale of stock. However, a corporate charter or stock restriction agreement may impose restrictions on the transfer of shares, as is often the case with closely held corporations.

Corporations differ from the other types of business entities in that corporations must pay income taxes on their profits, unless the corporation chooses to be treated as an S or Subchapter S corporation (the S or subchapter S refers to a provision in the federal tax code). Corporations that do not elect to be treated as an S corporation are called C corporations. C corporations are subject to what is called "double taxation." Corporate profits are taxed to the corporation when earned by the corporation and also taxed to shareholders as income if distributed to the shareholders as dividends. Many closely held corporations are largely able to avoid the adverse effects of double taxation by paying salaries to shareholders who serve as officers or employees of the corporation, interest to shareholders who lend the corporation money and/or rental payments to shareholders who lease land or equipment to the corporation (all of which would typically be an expense or tax deduction for the corporation).

S corporations, on the other hand, are pass-through entities where the corporation does not pay income taxes on profits. Instead, S corporation profits and losses "pass through" to the shareholders as they do in other types of business entities. Also like partnerships,

profits pass through to shareholders regardless of whether any dividends are distributed or not. However, unlike partnerships and sole proprietorships, the shareholder's share of profits from an S corporation is not subject to self-employment taxes. There are a number of restrictions on S corporations that are not placed on C corporations, including: S corporation shareholders must be U.S. citizens or residents; S corporations can have no more than 100 shareholders and only one class of stock, although there can be differences in voting rights; and corporations and partnerships cannot own stock in an S corporation. Typically, these restrictions do not pose too much of a problem for farms or other small businesses.

Corporations are also required to pay franchise and excise taxes to the state of Tennessee. The Tennessee excise tax is currently equal to 6.5 percent of the net earnings from business done in Tennessee for the tax year, while the franchise tax is currently equal to 0.25 percent of the greater of net worth or the book value of real or tangible personal property owned or used by the corporation, with a minimum tax of $100 per year.

Given that there are differences in corporate and individual income tax rates and which costs can be deducted from income earned, the effects of incorporation and/or election to be treated as an S corporation on income tax liability vary from one set of circumstances to the next. Thus, it is not necessarily true that an S corporation or other pass-through entity will result in a lower federal income tax liability than a C corporation. More information on the tax treatment of corporations can be found in the materials listed in the Additional Resources section of this workbook.

Thus, the primary advantages of the corporate form are limited liability for all owners (so long as the corporate formalities are observed), perpetual existence and the ease with which corporations can raise capital through the sale of shares of stock (which carry with them full voting rights). On the other hand, corporations are more costly to form and operate than sole proprietorships or general partnerships, as they require initial and annual filings and the payment of filing and annual fees as well as franchise and excise taxes. In addition, corporations may face a heavier tax burden than pass-through entities, unless the Subchapter S election is taken. While Subchapter S corporations come with some restrictions, these restrictions are unlikely to pose much of a problem for most farm and family businesses. The combination of limited liability and pass-through taxation has made Subchapter S corporations a popular choice for small businesses. However, the popularity of S corporations has recently declined due to a new type of business entity – the limited liability company.

Limited Liability Company

An increasingly popular choice for farms and small businesses is the limited liability company (LLC). LLCs are something of a hybrid, combining some of the most favorable attributes of partnerships and corporations into a single entity. For example, a LLC can elect to be taxed as a partnership while the LLC's owners can still enjoy limited liability and the right to participate in the management of the business. Further, the Tennessee law authorizing LLCs is designed to allow a great deal of flexibility in how an LLC is organized and operated.

Actually, there are two different sets of statutes in Tennessee authorizing LLCs. The first was adopted in 1994 and the second in 2005. The first governs all LLCs formed before January 1, 2006, unless the LLC chooses to be governed under the new law. The second governs all LLCs formed after January 1, 2006, as well as those formed earlier that elect to be governed by the new law. While there are a lot of similarities in the two sets of statutes, there are also substantial differences. Where there are differences, the following discussion will focus exclusively on the provisions in the new law. If one were to attempt to sum up these differences in a single concept, it would be that the new law provides even greater flexibility in LLC organization and operation. In fact, most of the provisions in the new statute for how LLCs are to be structured and operated can be waived by the LLC – thus they operate as default provisions for how the LLC operates absent agreement among the members to the contrary. This flexibility, while great for those wanting to custom design a LLC to fit their particular circumstances, makes it difficult to discuss LLCs as an option for farm and family businesses, since there are relatively few hard-and-fast rules.

In general, though, LLCs, like corporations, are separate legal entities distinct from their owners. Unlike corporations, LLC owners are typically referred to as members instead of shareholders. Unlike the restrictions imposed on shareholders in S corporations, LLCs have no limits on the number of members or the type of entity that can be a member. LLCs are formed in Tennessee by filing articles of organization with the Tennessee Department of State. The filing fee for the articles of organization is currently (2010) $50 per member, with a minimum of $300 and a maximum of $3,000. The Articles of Organization set out some basic information about the LLC but provide little information on its structure. This information is left to an operating agreement – the functional equivalent of a corporation's bylaws, but which unlike bylaws can be either oral or written. A written operating agreement is recommended. LLCs are required to file annual reports and pay annual fees currently equal to $50 per member, with a minimum of $300 and a maximum of $3,000. As these fees, and all other fees described in this chapter, may change over time, one should check with the Tennessee

Secretary of State for any changes and for a more complete record of the filing fees associated with LLCs or other business entities.

LLCs are also required to pay franchise and excise taxes to the state of Tennessee. The Tennessee excise tax is currently equal to 6.5 percent of the net earnings from business done in Tennessee for the tax year, while the franchise tax is currently equal to 0.25 percent of the greater of net worth or the book value of real or tangible personal

property owned or used by the LLC, with a minimum tax of $100 per year. However, LLCs that devote at least 66.67 percent of their activities to either farming or holding personal residences where one or more of its partners or members reside are exempt from franchise and excise taxes, provided application for the exemption has been made and approved by the Tennessee Department of Revenue.

LLCs are allowed great latitude in defining how they will be managed and what rights members will have. However, the Tennessee statute sets forth three different management structures that serve as models or templates of how LLCs can be structured. In a member-managed LLC, each member has equal rights in the management and conduct of the LLC's business and any matter relating to the business of the LLC is decided by a majority vote of the members. In a manager-managed LLC, each manager has equal rights in the management and conduct of the LLC's business and any matter relating to the business of the LLC shall be exclusively decided by the manager, or, if there is more than one manager, by a majority vote of the managers. Managers are appointed or elected by a majority vote of the members and need not be members of the LLC. In a director-managed LLC, all LLC powers are exercised under the authority of, and the business and affairs of the LLC are managed under the direction of, its board of directors. Any matter relating to the business of the LLC is exclusively decided by the director, or, if there is more than one director, by a majority vote of the directors. Directors are appointed or elected by a majority vote of the members and need not be members of the LLC. In addition, a director-managed LLC shall have a president who is appointed or elected by a majority vote of the directors and is authorized to act as an agent of the LLC. Thus, the member-managed LLC operates much like a general partnership and the manager-managed resembles a limited partnership, with the important difference that in both cases all members enjoy limited liability. Finally, the director-managed LLC operates much like a corporation.

LLCs can elect to be treated as either a pass-through entity, where the tax consequences of profits and losses pass directly through the LLC to the members, or as a corporation, where the LLC actually pays taxes on its profits and members pay taxes when they receive a distribution of profits. To conduct business in a state other than the one in

which they were formed, LLCs must obtain a certificate of authority from the secretary of state of such other state.

Although LLCs can be somewhat costly to start and operate, the benefits and flexibility they offer have made them a popular choice for small businesses. They can be structured to offer most of the advantages of both the corporate and partnership entities with few of the drawbacks. Thus, for LLCs, the question is often whether these advantages are worth the costs of creating and maintaining an LLC.

Cooperative

A final type of business entity relevant to farm operations is the cooperative. Cooperatives have been around for a long time and played an important role in the agricultural industry. However, their use was traditionally somewhat limited by rules designed to insure that they operated as a "cooperative venture" between individuals. However, the state of Tennessee recently authorized the creation of a new type of cooperative designed to be more attractive for investors and more applicable to modern agricultural production. Thus, there are now two types of cooperatives – traditional and new generation. Traditional cooperatives are businesses owned and controlled by the people who use them. They differ from other businesses in that the intent is to benefit their users rather than earn profits for investors. New generation cooperatives differ from traditional cooperatives in that they recognize the need for investment by people other than the users to finance modern value-added agricultural enterprises and, thus, allow for the participation of outside investors. However, cooperatives are generally not a viable option for the farm or family business. Thus, readers interested in learning more about cooperatives are advised to consult the materials listed in the Additional Resources section of this workbook.

Conclusion

This chapter considers the importance of choosing an organizational structure within the context of a succession plan. It focuses on the factors to consider when choosing a structure, paying particular attention to the different types of business or legal entities for farm and family businesses. The intent is to provide information on some of the basic, structural elements that go into a succession plan. An additional point to consider is that some succession plans or farm or family businesses might best include a combination of one or more of these legal entities or arrangements.

Regardless of which organizational structure is chosen, it is important to revisit the structure in the event of significant, unexpected changes in the operation of the

business, the circumstances in which the business operates or the circumstances of the individuals involved. Successful organizational structures often evolve over time as experiences, expectations and conditions change.

Finally, it is nearly impossible to overstate the importance of getting sound, well-informed legal and other professional assistance when needed. The material presented in this chapter and workbook can never substitute for the depth of experience and knowledge of a competent professional who is familiar with the unique circumstances relevant to a particular farm or family business. Thus, it is worth remembering that the goal of this chapter and workbook is to enable readers to play a more active role in the formation and evolution of succession planning for their farm or family business and be more sophisticated consumers of the legal and other professional services needed for this plan.

Table 4.1 Comparison of Legal 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 personal 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 upon owner's death	Dissolves upon death or withdrawal, unless continued by partners	Generally dissolves upon death, withdrawal	Perpetual existence	Generally dissolves upon death, withdrawal
Federal Taxation	Individual taxed	Pass-through entity – partners taxed	Pass-through entity – partners taxed	"C" - corporation <u>and</u> shareholders taxed "S" - pass-through entity, shareholders taxed	Pass-through entity – members taxed
Franchise and Excise Taxes	No	No	Yes, unless 66.7percent of activity is farming	Yes	Yes, unless 66.7 percent of activity is farming
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

Chapter 5: Estate Planning Tools

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Estate Planning

To control your property while alive, take care of your loved ones and yourself if you become disabled, and, upon your death, give what you have to whom you want, the way you want. And, if you can, save every last tax dollar, professional fee and court cost possible.

Some people think the only item a person needs to plan an estate is a will. However, a good estate plan includes a will and other documents to insure a person's wishes are carried out if he or she becomes disabled, incapable of handling personal affairs or if the person dies.

Most attorneys recommend a set of at least three documents be included in an estate plan. These are:

1. A will
2. A durable power of attorney (for finances)
3. Advanced care plan and health care agent

(also called a living will and power of attorney for health care)

The above and other tools and documents used in estate planning are covered in the following pages. However, all of the many laws and legal details of estates cannot be fully covered in this workbook. To insure your plan includes all the necessary components, you should hire an attorney who has additional training and experience in estate planning.

The Will

One common question is: Do I really need a will?

No law in Tennessee requires a person to have a will. More than one-half of Tennesseans die without a will. So do you need one?

YES, You Need One

- If you want to have any say in how and to whom those things you have spent your lifetime earning are transferred.
- If you want to name a guardian for minor or disabled children and name who would supervise the funds as the children are raised.
- If you want to donate to a charity, school or organization.

- If you want to name the executor of your estate and insure someone is not appointed by the court.
- If you want to minimize the expenses of probating the estate and reduce or eliminate taxes.
- If you want to provide for the continuation of a business or family farm.
- If you want to greatly reduce the stress and confusion caused when a will does not exist.

Advantages of Having a Will

1. Provide financial security for spouse and children.
2. Transfer assets as you want, not according to a state law.
3. Reduce / prevent income and estate taxes.
4. Establish who is the executor or personal representative of the estate.
5. Reduce expenses and possible time delays of settling the estate.
6. Name guardians for minor children.
7. Provide for heirs as you wish.
8. Reduce stress and confusion by heirs knowing your wishes.

No Will = Intestate

Intestate is the legal term for dying without a will. When there is no will, the state of Tennessee has laws, part of the "code annotated," which specify how the estate is distributed based on family relationships.

Many couples mistakenly think everything just goes to the surviving spouse. Most assets that are jointly owned with right of survivorship will transfer to a spouse or co-owner. Common examples are a joint checking account or a deed to the home that is owned as "joint tenancy with right of survivorship." Different estate tax rules apply for joint ownership with spouses as compared to co-ownership with anyone else. Most jointly held assets owned with a spouse transfer without any taxes owed. A joint asset co-owned with anyone other than a spouse will require one-half of the asset to be included in the value of the decedent's estate. Also, if a co-owner is added to a deed or account, a gift tax may be owed (see section on Gift Tax).

If there are children, state law specifies the percentage of all other assets that are transferred to them. Generally, without a will, a spouse inherits one-third or a child's portion, whichever is greater. So, if there is one child, the spouse and child would each receive one-half. If there are two or more children, the spouse receives one-third and

the children split the remaining two-thirds of the estate. Divorces and remarriages seriously complicate the issue. Without a will a current spouse may inherit assets originally intended to be given to children from a previous marriage or the opposite can occur.

Having no will can increase the expenses of probating the estate (probate information is covered later in this chapter). If there is no will to name the executor of the estate, either a family member can apply to the court to be appointed administrator of the estate (same duties as an executor) or the court will appoint someone to serve as administrator of the estate. An appointed administrator would be entitled to compensation for his or her work. However, the appointed administrator might not be the person you would have chosen. The lack of a will can increase the estate and income taxes owed. Far too often, family misunderstandings occur when there is no will to clearly state details concerning items promised to specific individuals during the decedent's (deceased person's) life. Without a will there is no document to insure what was promised goes to the intended person. Quite simply, there is no excuse for putting your family through the additional stress, confusion and expense caused when there is no will!

Contents of a Will

A typical will includes some standard sections. These include:

- Date the will is written
- Stating who wrote the will and that the person is of sound mind.
- Naming an executor(s), also called a personal representative, to handle the probating of the estate.
- Specifying if bonding of the executor is required.
- Specifying if an inventory of assets is required.
- Naming the beneficiaries who will receive assets of the estate.
- Listing any specific items, amounts or percentages of assets to be given to individuals or charities.
- A residuary clause to direct the distribution of all remaining assets. Residuary refers to the rest (residue) of the estate not specifically given to someone.
- Listing other wishes or duties to be carried out by the executor.

Types of Wills

There are many ways to write or create a will. Using a lawyer trained in estate planning law to help write your will is best. Also, having a properly prepared will can reduce the likelihood of the will being contested.

Hand-written or Holographic Will

A handwritten will can be recognized as a legal will. However, not knowing all the legal terms and items needed in a will could cause added expense when the will is probated. Even worse, it could possibly cause the will to be invalid. A holographic will must all be in the writer's own handwriting and must be signed and dated by the writer. Two individuals would have to verify in court that they are familiar with the deceased's handwriting and the signature belongs to the writer of the will before the estate could be probated. If a handwritten will is created during a time of illness or distress, it should be replaced with a formally prepared will as soon as possible and the holographic will should be destroyed.

Simple Will

A simple will names an executor and can provide for the distribution of assets to a spouse and children. It should also specify what happens if both spouses die together and if children die before parents. When no family exists a simple will can be used to direct the giving of assets to a charity, school, organization or to others.

Sweetheart Will

Sometimes called a "reciprocal will," "husband & wife will" or "I love you will," this type of will provides for everything to go to the remaining spouse. This type of simple will might not provide for children in case the surviving spouse remarries or becomes incapacitated.

Complex Will

A simple will might not be able to handle all the details in a more complicated estate. A more complex will may be needed in many situations.

- To transfer farm or business assets to heirs.
- To create a trust establishing funds for raising minor or disabled children.
- To transfer some assets directly to children to insure they receive a portion of the assets should the remaining spouse remarry or to prevent spending all the assets.

- To reduce or avoid estate tax.
- Other needs.

Pour-Over will

A pour-over will is often used to handle any remaining assets when a trust has been created to transfer the majority of the estate's assets. A pour-over will is commonly used with a living trust.

Assets Not Transferred by a Will

A will does not control some assets. Life insurance, IRAs, 401Ks and similar accounts with a named beneficiary transfer separately from a will. A will cannot override the named beneficiary. Other jointly held property, such as land with a deed listing a husband and wife as joint tenants with right of survivorship, would typically transfer directly to the surviving spouse. Another example includes jointly owned bank accounts, which would also transfer to the surviving spouse or co-owner. Also a bank account with a payable on death (POD) designation listing a person to which it is payable would transfer directly.

Power of Attorney

A power of attorney (POA), often called a durable power of attorney, allows a person to handle your financial matters. These are commonly created when a person is about to undergo major surgery or who has reason to think he or she might have limitations in the future or as a precaution as someone ages. A person should not wait until an event occurs to create and name a POA. Often when a POA is needed, a person may already be unable, due to injury or disability, to name one. If no POA has been executed and a disable person requires management of his/her assets, a petition must be filed with the court for the appointment of a conservator. This process can cost thousands of dollars in legal and court fees, can take several months to complete, and is quite a hassle for families already dealing with an ill loved one.

The person selected must be someone trusted to handle finances as you would have desired. The power of attorney can be written to limit or restrict the power of the named POA. For example, the POA could be given the power to pay bills and handle bank deposits, but the POA would not be allowed to sell or trade real estate or other assets. Two important facts about powers of attorney:

1. A POA is effective when written, meaning the person named as POA has the right to exercise it immediately. If you don't want the POA to take place at once, one

option is to write a “springing” POA, which becomes effective when a doctor has certified the writer of the POA is incapable of managing his or her affairs. One issue with a “springing” POA is that some doctors are hesitant to provide such certification. The “springing” POA must authorize the doctor to release such medical information.

2. A power of attorney’s authority ends at your death. The person named as your POA has no rights or power to transact business on your behalf upon your death. Power after death is given to the executor of the estate named in your will after proper appointment by the court.

Advance Care Plan (also called a living will or medical directives)

An **advance care plan** allows you to have written directions for your medical care if you are not able to make your own choices. Having an advanced care plan helps eliminate confusion about the level of medical care you want if you are in a coma, injured and can’t respond or have a terminal condition. You can specify the level of care desired in a variety of medical situations. Preferences like organ or tissue donation can be included in the advanced care plan so doctors and family members know your wishes.

The term **advance care plan** was clarified in Tennessee state law to reduce confusion between similar terms. A related term is **health care agent,** which had been called a power of attorney for health care or health care proxy. The health care agent would help doctors and family members make decisions concerning your care. Your health care agent should be someone who understands your wishes and would have the stamina and backbone to deal with doctors and family should tough decisions need to be made.

The Tennessee Department of Health provides a set of blank forms on its Web site (http://health.state.tn.us/AdvanceDirectives/index.htm) to help people create their advance care plans. A copy is also provided in the appendix for Chapter 5 of this workbook. It is recommended that you have both an advanced care plan and that you name a health care agent. An attorney is not required for either of these. A copy of the advanced care plan should be provided to your doctor, health care agent and any hospital or medical facility where treatment is received.

Trusts

A trust is a legal agreement naming a person as a "trustee" of the assets included in the trust. As the creator of the trust, you are the "trustor" or "grantor." The trustee manages the assets according to the directions provided in the trust to benefit the "beneficiaries" of the trust. Some trusts are created in advance and others are created by a will. When a will transfers assets upon death, a trust can be effective immediately. A common use of a trust is to provide the funds for the raising of minor or disabled children should both parents die. Trusts are also used to provide for the continuation of a farm or business, so funds are readily available for the business to continue operating during the probate process. Trusts can be used to reduce the value of an estate to an amount close in value to the federal or state estate tax exclusion. A trust may better protect assets from a lawsuit or other legal action, where a will might not provide such protection because a trust more clearly establishes the beneficiaries of the assets and names a trustee to oversee the handling or distribution of the assets.

Testamentary Trust

Any type of trust created in a will is referred to as a testamentary trust. One of the main types of testamentary trusts is one to reduce estate taxes and preserve income for the surviving spouse. This type of trust becomes effective upon the first spouse's death. These trusts do not save probate fees, because upon the death of the first spouse, his or her will directs the establishment of the trust. The assets placed in the trust can generate income for the surviving spouse while qualifying for the estate tax exemption and/or marital deduction to reduce or eliminate estate taxes upon the death of the surviving spouse. Two types of testamentary trusts called a "bypass trust" or "A-B trust" provide for full use of the estate tax exemption by both spouses to reduce or eliminate estate tax. Another type of testamentary trust is a "family trust," which can be used to transfer assets to children or other heirs rather than a spouse. Smaller estates may not benefit tax-wise by creating a testamentary trust.

Other testamentary trusts include those that provide for the management of assets for minor children until the children reach a designated age or ages. Testamentary trusts may also be used for adult children for asset protection or generation skipping.

Living Trust

A common type of trust called a living trust is created while the trustor is alive, unlike a testamentary trust that is created by the will. Living trusts are often created as a revocable living trust, because a person can amend or revoke it anytime during his or her lifetime. The trustor retains absolute control over the assets of the trust. Upon the trustor's death, the living trust becomes irrevocable. It either terminates, with the

assets going to the designated beneficiaries, or it continues, with the trustee managing the trust assets for the beneficiaries. A revocable living trust can be changed, modified or discontinued at any time during the lifetime of the trustor.

Living trusts are often promoted inaccurately as a means of eliminating the need for probate. To prevent probate, ownership of all assets would have to be transferred to the trust. Any assets owned outside the trust would still require the probate process to transfer to an heir. The creation and maintenance of a living trust are generally much more expensive than a will. A revocable living trust can have the same tax planning as wills. Some people use high-pressure sales tactics to scare people into buying expensive living trusts that are not needed to properly transfer property. Often a much less expensive will could accomplish the same objective. It is important to get good legal advice about living trusts.

Irrevocable Trust

An irrevocable trust is created during the trustor's lifetime to remove assets or property permanently from the estate. Putting assets in an irrevocable trust is final. The assets cannot be reclaimed and the trust conditions cannot be changed once established. The assets in the irrevocable trust would not be included as part of the estate. They are often used to purchase life insurance. Any transfers to an irrevocable trust are gifts and gift tax consequences must be considered.

Charitable Remainder Trust

A charitable remainder trust (CRT) can be a testamentary trust or an inter vivos (liftetime) trust. A CRT can be established to transfer assets to a charity while retaining an income stream during your and your spouse's lifetime. Upon the death of the spouse or the end date of the life of the trust, the asset(s) would pass to the charity. The value of the remainder interest is deductible for income tax purposes in the year of the gift. They can also be set up with children as the income beneficiaries.

Other Trusts

Many other types of trusts are useful in estate planning. A life insurance trust, generation-skipping trust and others may be valuable in planning and reducing income and estate taxes. Before choosing any trust, thoroughly research its usefulness and seek assistance from legal and financial advisors.

IRAs and 401Ks

One of the most important estate planning items often overlooked is naming a beneficiary of your IRA, 401K or similar retirement investment account. You may name

one or more people as the beneficiary of your IRA or 401K. Substantial tax dollars may be saved by naming a beneficiary. It is best to name both primary and secondary beneficiaries. Be sure to change beneficiaries if a beneficiary should die or in the case of divorce.

Depending on the age of the decedent and if distributions from the IRA or 401K had begun, the required minimum distributions (RMI) from the account may be recalculated to spread the payments over the beneficiary's lifetime rather than the previously calculated lifetime of the deceased. The beneficiary may have other options for receiving the funds, depending on the plan and IRS rules. Naming one or more beneficiaries prevents the IRA or 401K from becoming part of the probate estate, so that a lump sum distribution may be avoided and income taxes greatly reduced. When the estate receives IRA or 401K funds, they are considered income to the estate, and the estate will have to pay income taxes on this income. The income tax rates for estates are typically much higher than for individuals. Retirement assets are still assets of the deceased subject to estate taxes. Consult your financial advisor concerning your IRA or your employer concerning your 401K to ensure you have one or more beneficiaries listed.

Gift Taxes

Federal Gift Tax

Gifting assets can be a valuable estate planning tool. Gifting can help reduce the value of the estate and reduce potential estate taxes. Of course, only unneeded assets should be gifted.

Current (2010) federal law allows any person to give away up to $13,000 per year to as many people as he or she wishes, free of any gift tax or reporting. A husband and wife can give up to $26,000 per year per person of jointly owned assets (equals $13,000 each). If these levels are exceeded, a gift tax return (Form 709) must be filed. This does not necessarily mean a federal gift tax would have to be paid.

Currently, every person has a federal lifetime gift exclusion of up to $1 million. Any gift exceeding the $13,000 per person annual exclusion reduces the individual's lifetime $1 million exempted amount.

Tennessee Gift Tax

The Tennessee gift tax is calculated differently from the federal gift tax. There is the annual $13,000 exclusion. But, any amount gifted each year in excess of $13,000 will

cause a gift tax to be due. Tennessee gift tax also varies, based on whether the recipient is a Class A or Class B beneficiary (see below). The annual exclusion is lower for Class B beneficiaries. Tennessee gift tax rates range from 5.5 to 16 percent, depending on the amount of the gift and the class of beneficiary. See the Tennessee Department of Revenue Web site (http://tennessee.gov/revenue/tntaxes/gift.htm) for more information.

Class A *- Husband, wife, son, daughter, lineal ancestor, lineal descendant, brother, sister, son-in-law, daughter-in-law or stepchild. If a person has no child or grandchild, a niece or nephew of such person shall be a Class A beneficiary.*

Class B *- Any other relative, person, association or corporation not specifically designated in Class A.*

Other potential gift tax situations can occur when a person is added to a deed or is added as a co-owner of a bank account. Either of these events would be the same as giving one-half of the value of the land or account to the new joint owner and could cause gift taxes to be owed. Another common mistake is toexecute a quit claim deed to transfer property to a child or other person keeping a “life estate” in the property, meaning you get to use the land until your death. This is equal to giving the property to the individual and could require federal reporting of the gift and possibly substantial gift taxes to be owed to the state of Tennessee. A tax accountant or estate attorney should be consulted to help with gift planning to prevent taxable situations. Gifting also impacts the eligibility for Medicaid (see the section on Medicaid Planning).

Other Planning Tools

Conservation Easements

Conservation easements have become popular in recent years as a way for farm and land owners to insure their land will be used for farming, recreational or wildlife purposes forever by placing a conservation easement on the deed to the land. This change prohibits all future owners of the land from developing the land for any purpose other than those stated in the conservation easement agreement. The following paragraphs help to explain what a conservation easement is, how one works and the possible tax advantages.

What Is a Conservation Easement?

A conservation easement (or conservation agreement) is a legal agreement between a landowner and a land trust (or other qualified agency) that permanently limits uses of the land to protect its conservation values. It allows you to continue to own and use

your land and to sell it or pass it on to heirs while keeping the land free from development.

When you donate a conservation easement to a land trust, you give up some of the rights associated with the land. An easement on property containing rare wildlife habitat might prohibit any development, for example, while one on a farm might allow continued farming and the building of additional agricultural structures. An easement may apply to just a portion of the property, and does not require public access.

Usually conservation easements are donated. If the donation meets federal tax code requirements, it can qualify as a tax-deductible charitable donation. The amount of the donation is the difference between the property's value with the easement and its value without the easement.

Perhaps most important, a conservation easement can be essential for passing land on to the next generation. By removing some of the land's development potential, the easement lowers its market value, which in turn lowers estate tax. Whether the easement is donated during life or by will, it can make a critical difference in the heirs' ability to keep the land intact and avoid having to sell a portion of the property to pay estate taxes.

How Can Conservation Easements Help with Estate Planning?

> "*The estate tax remains part of the U.S. Tax Code in spite of years of efforts to repeal it. It weighs particularly heavily on people whose primary asset is land, such as farming families. This is because land, which is the principal asset of such families, represents taxable value, and in many parts of the country, land has increased in value out of all proportion to its value for agricultural use. However valuable land may be, it is not easily liquidated to pay taxes, and where the land in question is the family farm, liquidating to pay estate taxes can force an unwanted and significant change in lifestyle. For families who want to keep their land intact, and for who land is a primary asset, a conservation easement may make the difference between keeping the land and being forced to pay estate taxes.*"
> Lindstrom, C. Timothy. A Tax Guide to Conservation Easements. Washington, DC: Island Press, 2008.

There are many ways that conservation easements can result in substantial estate tax savings. Here are some examples:

1) Reduction in value of the estate: Any land subject to a conservation easement included in the estate is valued as restricted by the easement and not as the unrestricted value.

A simple example: Farmer Joe's farm is worth $5 million because it is in an area of increasing residential development. Farmer Joe places a qualified conservation easement on his farm in 2005, reducing the value of his farm to $1 million. In 2009, Farmer Joe passes away, leaving the farm as part of his estate. The conservation easement has reduced the value of the estate by $4 million.

Note: The reduction in value of a landowner's property due to a conservation easement may be much greater when he or she dies than when the easement was originally donated, because land values have most likely appreciated since the conservation easement was conveyed. As the development potential eliminated by a conservation easement appreciates, the reduction in value attributable to the easement, and therefore the estate tax savings, also increases. (Lindstrom, C. Timothy. A Tax Guide to Conservation Easements.)

2) The 2031(c) Exclusion: This section of the federal tax code says that if you die owning land subject to a conservation easement, in addition to the reduction in land value because of the easement, the estate can take an additional exclusion of 40 percent of the already reduced land value.

Simple example: Remember Farmer Joe from above. His farm was worth $1 million at his death because he donated a conservation easement during his lifetime to the local land trust. Under 2031(c), Farmer Joe's executor can elect to exclude 40 percent of the restricted value of the farm from the estate. Therefore, an additional $400,000 (1 million x 40 percent) can be excluded from the estate.
Notes:

- The 2031(c) exclusion is capped at $500,000 no matter what the value of the land is subject to the conservation easement.
- The 2031(c) exclusion applies to land value only, not the value of the structural improvements on the land.

- The 2031(c) exclusion only applies to easement-protected land that has been held by the landowner or a member of his or her family for at least three years prior to the landowner's death.
- The 2031(c) exclusion benefit is available to each succeeding generation of landowners as long as the land remains in the family and is not sold to a person outside the family.

3) Conservation easements by will: Landowners who are reluctant to donate a conservation easement during their lifetime can always consider a conservation easement by will. Conservation easements contributed by will are not eligible for federal income tax benefits but are eligible for an estate tax deduction, similar to those discussed above.

Notes:

- Landowners considering a conservation easement created by their will should discuss their intentions with the land trust that they would like to hold the conservation easement. Most land trusts prefer to have the conservation easement drafted in advance and attached to the landowner's will (or at a very minimum, the will should contain specific language about the conservation goals of the landowner). This will make the process much easier for the land trust and the executor of the estate upon the death of the landowner.

4) Post-mortem conservation easements: Section 2031(c) of the Federal Tax Code also allows for a unique estate planning tool – the post-mortem conservation easement. If a landowner owns conservation-worthy land at the time of his or her death, this provision allows a family or executor to place a conservation easement on the land after death or post-mortem. A post-mortem conservation easement allows an estate to reap the same estate tax benefits (mentioned above) that would be applied had the conservation easement been donated during the lifetime of the landowner.

Notes:

- A post-mortem conservation easement must be completed prior to the due date for the estate tax return (typically nine months after the date of the landowner's death)

Post-mortem conservation easements only qualify for estate tax benefits if no income tax deduction is taken in connection with the donation

Information summarized from: Lindstrom, C. Timothy. A Tax Guide to Conservation Easements. Washington, DC: Island Press, 2008

Federal Estate Tax Example (updated for 2009 estate tax rates)
Situation:
Farmer Jane dies owning 200 acres of farmland in Maury County, Tennessee. Her farm is worth $4,000,000 and she has $200,000 in savings. She has 2 children and she leaves the farm to them in her will.

Example 1: No conservation easement donation
Total estate value in 2009: $4,200,000, Total estate tax that children will have to pay upon inheritance: approximately $229,800 (after $3,500,000 exclusion, tax is calculated on $700,000. See table on federal estate rates in this chapter.)

Example 2: Conservation easement donation
Farmer Jane placed a conservation easement on her farm in 2006 and lowered the value of the farm to $1,000,000. So total estate is now valued at $1,200,000 (instead of the $4.2 million above) Total estate tax that children will have to pay upon inheritance: $0

(In 2009, only estates valued at more than $3.5 million are subject to federal estate tax. Tennessee inheritance tax will still be owed if over $1,000,000.)

2031(c) - additional estate tax savings:
Remember, 2031 (c) says that if you die owning land subject to a conservation easement, in addition to the reduction in land value because of the easement, the estate can take an additional exclusion of 40 percent of the already reduced land value (exclusion is capped at $500,000)

Example:
$3,000,000 (Jane's farm unprotected)
-2,000,000 (the easement value)
= $1,000,000 (the 'after' value)
- 400,000 (the 40% exclusion: $1 million x 40%)
=$600,000 (NOT TAXED AT A FEDERAL OR STATE LEVEL)

Author's Note: The above section on conservation easements was provided by the Land Trust of Tennessee. They are one of only a few organizations in Tennessee that accept and manage conservation easements. Through funding provided in part by the state of Tennessee they can provide land owners with planning and financial assistance with some of the expenses involved in creating a conservation easement. The above examples only consider the potential estate tax savings. Current tax laws may provide additional income tax savings when conservation easements are placed on property prior to death of the owner.

Life Insurance

Life insurance can be used in many ways as part of an estate plan. Some of these are:

- An individual may purchase life insurance to provide funds for the surviving spouse or children.
- A whole life policy may be purchased to provide income during retirement by converting the policy to an annuity or withdrawing the cash value.
- Insurance dollars may be passed as an inheritance to non-farm or non-business heirs. This allows farm assets to flow to farming heirs. The insurance dollars allow all heirs to receive something while preserving an intact farm or business.
- Insurance funds may be used to pay death taxes, estate settlement costs or debt obligations.
- Farming heirs may purchase life insurance on their parents to provide funds for purchase of farming assets from other heirs.
- Farming partners may use insurance funds to insure an operation could continue if one partner dies prematurely.
- Insurance may simply be used to create or enhance an estate.

Disability Insurance

Often, families suffer financially when one spouse is injured or becomes disabled due to illness. The loss of income and additional medical expenses can greatly change the family's financial situation and the ability to stay in business. Purchasing disability insurance can provide income should one spouse become disabled and may prevent having to make difficult financial choices while under the stress of a physical or mental impairment.

Long-term Care

The cost of care in a nursing home is a major concern. Nursing home costs currently range from $150 to $250 per day ($54,750 to $91,250 per year) for room and board plus medicine and doctor visits. The drain on a lifetime of savings can be considerable. Purchasing long-term care insurance to offset part or all of this potential expense could insure there will still be assets for heirs to inherit. Depending on your age, the monthly cost of a long -term care policy can be significant. Figuring the monthly cost of coverage against the substantial cost of nursing home care may require much family discussion.

Current health situation, family health history and financial situation all play a part in the decision process.

Many companies offer long-term care insurance to provide funds should a person become a patient at an assisted living facility or nursing home. Some policies also cover the cost of in-home care. The cost and potential payout from these policies vary widely. Most policies provide coverage for three to five years of care. It is wise to carefully research long-term care policies to get the best value. One factor that can increase the monthly cost of long-term care insurance is if the policy adjusts future payments based on inflation. For example, a policy might pay $150 per day for nursing home care today, but the amount would be adjusted each year for inflation. The policy would pay more in the future to provide basically the same coverage. Policies with this inflation adjustment capability will cost more than a policy with a flat monthly payment rate that does not change. Policies vary and it is important to work with a professional to understand what you are purchasing.

Funeral / Burial Prepayment

Most funeral homes and memorial gardens have prepayment plans or types of burial insurance to cover the costs associated with funeral services and internment into a grave or cremation. Most of these plans allow you to select the types of services, casket or cremation service and possibly even a monument. Be certain of the expenses covered in any plan. Items such as the digging and covering of a grave (called opening and closing) can cost $300 to $600 and might not be included in all plans if an outside contractor is used. Having the ability to transfer the prepayment plan to a different funeral home can be a valuable option.

A prepaid plan with most of the choices made reduces the stress on family members who must make decisions during a very stressful time. Often, families overspend, thinking it is what the deceased would have wanted or because of their desire to honor the deceased. By prepaying, you have made the choices and covered most of the expenses for them.

Medicaid Planning

Medicaid is a state / federal program for paying nursing home expenses for people with limited income and few assets. The rules for qualifying for Medicaid are quite stringent and require most of the assets of the individual or couple to be spent for care before Medicaid qualification requirements are met. Good planning can assist with qualifying for Medicaid sooner.

Many people transfer assets to family members to reduce the value of the estate, allowing them to qualify for Medicaid. The rules and possible penalties are very specific with regard to transferring assets to qualify for Medicaid. The "look-back" rules on transfers used to be 36 months, but any type of asset transfer after February 8, 2006 has a look-back period of 60 months. Generally, if a person is qualified in all other ways for Medicaid, but had a transfer during the look-back period, there is a formula to determine how long the Medicaid is delayed in beginning. Each state calculates the formula to be the value of an average monthly cost in a nursing home divided into the value of the asset transferred. Additionally, transferring assets may generate gift taxes.

Example: Assume that a person qualifies for Medicaid in all other ways. If an asset worth $50,000 had been gifted during the look-back period, and the average monthly nursing home cost is $3874, then 50,000 divided by 3874 equals 12.9. Medicaid payments would be delayed by 13 months. Failure to report asset transfers occurring within the look-back period can result in criminal fines and penalties, and could cause the state to force sale of a gifted asset to reimburse the state for Medicaid expenses. Most qualified estate attorneys can include assistance with Medicaid planning as part of an estate plan. The federal gift tax exemption could be used, but Tennessee gift taxes would be due.

Letter of Last Instructions

Another document that can provide information about your wishes and much stress relief for family members is a letter of last instructions. This letter could be provided in advance to your lawyer, executor, spouse or other family members. The letter of last instructions can include:

1. Names, addresses and telephone numbers of those who should be notified of your death.
2. Instructions for your funeral and burial or cremation and memorial service.
3. Location of your will.
4. Location of your safe deposit box and its key, and a list of its contents.
5. Location of your essential personal papers.
6. Location of life, health, property and burial insurance policies.
7. Location of papers for pension or retirement plans, IRAs, etc.
8. Location of membership certificates to unions, lodges or fraternal organizations that provide death or cemetery benefits.

9. List of personal and real property you own, i.e., checking and savings accounts, all real property and location of deeds, stocks, bonds or other securities, business property, location of titles or other records.
10. Location of any separate list of how you want tangible property distributed after your death.
11. Location of income tax returns and supporting documents.
12. Location of all credit cards.
13. Location of any trust funds, names of trustees and copies of trust fund agreements.
14. Names of advisors such as your lawyer, banker, insurance representative, broker, accountant or tax advisor.
15. Your father's full name and mother's full maiden name, which are needed for the death certificate.
16. Instructions and directions concerning your business.
17. Other instructions as needed.

Federal and State Estate Tax Exclusion Amount (as of 8/17/09)

Year	Federal Exclusion	Tennessee Exemption
2000-2001	**$675,000**	**$675,000**
2002-2003	**$1,000,000**	**$700,000**
2004-2005	**$1,500,000**	**$850,000-$950,000**
2006-2008	**$2,000,000**	**$1,000,000**
2009	**$3,500,000**	**$1,000,000**
2010	**$0 -????**	**$1,000,000**
2011	**$1,000,000 - ????**	**$1,000,000**

It is expected congress will pass legislation during 2010 to retroactively maintain the federal exclusion at $3,500,000 for 2010 and future years.

Federal Estate Tax Rates

FOR A TAXABLE ESTATE		THE FEDERAL ESTATE TAX	
From	**To**	**Is**	**of Amount Over**
$0	**$10,000**	**18%**	**$0**
10,001	**20,000**	**1,800 + 20%**	**10,000**
20,001	**40,000**	**3,800 + 22%**	**20,000**
40,001	**60,000**	**8,200 + 24%**	**40,000**
60,001	**80,000**	**13,000 + 26%**	**60,000**
80,001	**100,000**	**18,200 + 28%**	**80,000**
100,001	**150,000**	**23,800 + 30%**	**100,000**
150,001	**250,000**	**38,800 + 32%**	**150,000**
250,001	**500,000**	**70,800 + 34%**	**250,000**
500,001	**750,000**	**155,800 + 37%**	**500,000**
750,001	**1,000,000**	**248,300 + 39%**	**750,000**
1,000,001	**1,250,000**	**345,800 + 41%**	**1,000,000**
1,250,001	**1,500,000**	**448,300 + 43%**	**1,250,000**
1,500,001	**2,000,000**	**555,800 + 45%**	**1,500,000**
2,000,001	**& Up**	**780,800 + 45%**	**2,000,000**

Tennessee Inheritance Tax Rates

Net Taxable Estate	Tax Rate
Not over $40,000	**5.5%**
$40,000 - $240,000	**6.5%**
$240,000 - $440,000	**7.5%**
Over $440,000	**9.5%**

Probate

Probate is the legal process to distribute the estate according to the provisions of a will or according to state law when there is no will. The probate process is not highly complicated, but many use the expertise of an attorney to oversee the probate process, especially with large estates, to insure all details are handled properly. Most courts require attorney representation of the executor.

Probate includes a number of steps. While not all are necessary in all estates, the steps may include:

1. Petition to the court to probate the will or administration of the estate.
2. Appointment of the executor (executor is sworn in, often by court clerk).
3. Notice to creditors (usually a newspaper advertisement provided to the local paper by the court clerk and covered in the probate fee)
4. Securing of bond by executor, if required.
5. Assembly, inventory and appraisal of property (if required or needed).
6. Classification and payment of demands against the estate (such as debts and liens against the decedent's property).
7. Management (and sale if necessary) of property.
8. Payment of state and federal taxes (filing of tax returns).
9. Accounting to the court and distribution of property.

Most of the probate steps are handled directly by the executor or administrator. An executor is called a personal representative in some states. The duties of the executor include:

1. Proves the will in probate court by providing the original copy of the will to the court clerk to be verified by a judge, who allows the opening of the estate and beginning of the probate process.
2. Secures copies of death certificates.
3. Establishes estate bank account(s) to handle funds.
4. Collects and inventories assets and property.
5. Pays bills and collects debts.
6. Files tax returns.
7. Manages probate property; converts property to cash if needed.
8. Defends or brings lawsuits, if necessary.
9. Distributes property.
10. Files final accounting with court, makes distribution to beneficiaries/heirs, and closes estate.

Most probate courts desire the estate probate process to be completed within 12 months or less. The size and complexity of the estate may lengthen the probate process. When choosing an executor, you should select someone who is capable, willing, able to keep peace among family members, able to meet legal requirements and located nearby, if possible.

Probate is not expensive when additional legal assistance is not required. The opening of the estate to begin the probate process in most Tennessee counties costs between $300 and $400. Costs may be higher when local newspapers charge higher rates to print the notice to creditors. Often, when a family member serves as executor, he or she is not paid for doing so other than for reimbursement of expenses, but an Executor can take a fee. When no will exists and the court appoints an administrator, the administrator is entitled to compensation for his or her work. Executors and administrators might receive 3 to 5 percent of the value of the estate as compensation depending on the size and complexity of the estate and depending on court rules or guidelines.

Some assets do not transfer through the probate process. Assets owned by joint tenancy with right of survivorship, joint bank accounts and payable on death (POD) accounts

would all transfer directly to the joint owner or named person. Assets in a trust transfer according to the trust document. Beneficiaries of life insurance would receive the proceeds of the policy. Beneficiaries of IRAs, 401Ks and similar retirement accounts would become owners of those accounts and would be required to follow IRS rules concerning the distribution of the funds. There are major income tax advantages to the estate and the beneficiary when the retirement accounts transfer directly outside of the estate.

A "Sample Attorney Estate Planning Questionnaire" is included in the appendix for Chapter 6 of this workbook. This form provides a sample of the type of information an attorney will need to begin the process of writing your will and developing your estate plan. Your attorney may require additional information depending on the complexity of the estate. This topic is covered in more detail in Chapter 6.

Chapter 6: Finding and Working with Professionals

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Professional Services Needed in Succession Planning

Preparing a satisfactory succession plan will often require the assistance of one or more professionals. Whether a single professional will suffice or whether a team of professionals is needed will depend on your particular circumstances. Most succession plans will benefit from the services of an attorney who is familiar with retirement, estate planning issues, and entity formation. An accountant may also be needed to help with the preparation of income tax returns and financial record-keeping. Individuals or families engaged in succession planning should also consult their agent to verify their insurance coverage is adequate for their needs and will continue to meet these needs in the future. Many families also rely on a financial planner to help formulate and achieve financial goals and manage investments and other assets. Bankers, loan officers, appraisers and foresters may also help collect and provide information for the succession plan and assist in financial planning. Finally, in some instances a professional mediator or counselor may be needed when there are difficult personal issues to be overcome.

After identifying which professional services are needed, the next step is to identify the professionals who can adequately and cost-effectively provide these services. Bankers, insurance agents and financial planners are often associated with a particular company, so choosing one may be as much about choosing the company as it is about choosing the person. Also, many families engaged in succession planning may already have existing or even long-standing relationships with a banker, financial planner, insurance agent and accountant. In these instances, the issue is not of finding and choosing a particular professional, but of making sure that the individual is qualified to provide the services needed for the succession plan and to adequately involve the individual in the succession planning process. Given these factors and the importance of legal services to the succession planning process, the rest of this chapter focuses on finding and selecting an attorney and establishing a productive attorney-client relationship with this individual. However, much of what is said often applies to the providers of other professional services as well.

Finding and Choosing an Attorney

The first question many people have is: "How do I find and choose an attorney to assist with my succession plan?" As most attorneys now advertise in one form or another, finding attorneys is not particularly difficult. The Yellow Pages and a Web search are likely to provide a reasonably complete list of attorneys in a particular location. The more difficult step is determining which of these attorneys is right for you. The practice of law is so broad and varied that no lawyer can be an expert in every field of law. Some attorneys have a broad practice that includes a large number of different practice areas, while others focus more specifically on a fairly narrow range of topics. If you are only looking for an attorney who can draft a simple will, then someone without a great deal of experience and expertise in estate planning may suffice. On the other hand, if you are looking for someone to help you craft a more complex succession plan, you may be better served by an attorney who focuses almost exclusively on estate or succession planning.

Advertisements in the Yellow Pages or on Web sites often list an attorney's areas of practice. Since there are no specific criteria an attorney must meet before he or she can list estate planning, wills, trusts or probate as an area of practice, these advertisements should be taken with a rather large grain of salt. However, the number and range of different practice areas advertised may provide a good clue as to the extent to which the attorney specializes in any one particular area. Advertisements may also claim specialization in a particular legal area. In Tennessee, attorneys who have passed a written examination on estate planning, practiced estate planning for a number of years and currently devote a significant part of their practice to estate planning can be certified by the Tennessee Commission on Continuing Legal Education and Specialization as a specialist in estate planning. While an attorney does not need to qualify as a specialist in estate planning to provide competent or even excellent estate planning legal services, you can be assured that attorneys who do qualify have proven experience and expertise in this particular area.

Another more objective resource for locating attorneys and finding out about their areas of practice and qualifications is the *Martindale-Hubbell® Law Directory*. By consulting this directory, you can find out an attorney's age and place of birth, how long they have practiced law in Tennessee, where they attended law school and the legal areas in which they practice. In some instances, the directory also provides a rating of the attorney's legal ability, as determined by other attorneys in the city in which they

practice. The directory is available on the Internet (http://www.martindale.com/), in law school libraries and, possibly, in your local public library.

A second way to find an attorney is through a lawyer referral service. These referral services are operated by the bar associations in Knoxville, Chattanooga, Nashville and Memphis. For a small fee, usually around $25–50, the staff of the lawyer referral service will arrange an appointment between you and an attorney who practices in the area of law in which you need assistance. The date and time of the appointment will be scheduled during your initial call to the lawyer referral service. The fee covers your first 30-minute consultation with the lawyer. This 30-minute consultation can help you explore the attorney's suitability, determine the approximate cost for his or her services and estimate how long the entire process will take. Contact information for these referral services is provided in the Additional Resources section of this workbook.

Word-of-mouth can also be an effective way to not only locate attorneys who practice in estate planning but also get an idea of how these attorneys have performed for other clients. Thus, it is often helpful to seek advice from people who have gone through the succession planning process or from other professionals who may have had an opportunity to work with attorneys in this context. However, you should be cautious about any recommendations that come from someone who might have a personal reason to recommend one lawyer over another.

Finally, after you have identified one or more attorneys who appear to be capable of providing the services you need, you should verify that they are in good standing with the Tennessee Board of Professional Responsibility (TBPR). You may do so by either calling the TBPR at (800)486-5714 or by visiting it online at www.tbpr.org. If there are no disciplinary problems, the next step is to schedule an initial meeting or consultation to determine whether they really are the right attorney for you.

Preparing for Your First Meeting

The first meeting between you and an attorney offers the two of you an opportunity to get to know each other and determine whether he or she is the right person to handle your estate planning needs. You should come to the meeting prepared to evaluate the attorney's qualifications and to give the attorney an overview of your needs. However, it may be a good idea to let the attorney guide the conversation at least initially so that he or she can evaluate your needs before being asked to respond to your questions.

Questions to Ask Before You Hire an Attorney

- How much experience do you have in estate planning?
- How much of your estate planning work has involved farm or family businesses?
- What percentage of your practice involves estate planning work?
- What alternatives will be considered in preparing my estate plan?
- What problems do you foresee in preparing my estate plan?
- Do you have any conflicts of interest that I should know about before I hire you?
- What documents will be prepared and approximately how long will it take to prepare them?
- How will you keep me informed of progress?
- What hourly rate will you charge and how often will you bill me?
- What other costs or expenses will I be responsible for paying?
- Who else in your office will work on my case?
- Can paralegals or more junior attorneys handle some of the work at a lower rate?
- What is a ballpark figure of my total bill, including all fees and expenses?
- Would you consider doing the work for a flat fee?

Some attorneys may ask you to complete a questionnaire and provide you with a list of documents to either bring with you to the first meeting or to send ahead of the meeting. If not, it is still a good idea to collect some information and documents to take with you to the first meeting. Being thorough in the collection and organization of this information will save you money and time and may improve the quality of the services the attorney is able to offer you. It also sends a message to the attorney that this matter is important to you and that you expect it to be treated with importance. Also, you understand the value of your attorney's time and expect that your attorney will be efficient in the delivery of his or her services.

Documents to bring to the first meeting:

- Business plan or summary of information about your farm or family business, including a diagram or organizational chart of the business, if needed.
- Written proposal of your transfer plan.
- Balance sheet, including assets and liabilities owned by you or any entities that are wholly or partially owned by you. Any asset inventory or other records that indicate the value of these items may also be useful.
- List of owners or directors of such entities, along with recent tax returns, financial statements and corporate records for these entities.
- Your complete personal income tax returns for the last three to five years.
- Legal description of any real property in which you have an interest. You can find the legal description in the deed, mortgage or deed of trust, or abstract or title insurance policy.
- Copies of:
    - Mortgages or deeds of trusts covering any real property wholly or partially owned by you or any entity wholly or partially owned by you.
    - Any leases of real or personal property.
    - List of oral agreements you have with a creditor, landlord, tenant or other party.
    - Financial statements you may have given to anyone in the past two years.
- List of anyone who owes you money or to whom you owe money, along with their addresses, the amount owed, the terms of the loans and any documents related to the loans.
- Marital agreements and/or divorce decrees.

Finally, it is important to be honest and forthcoming in the information you provide to the attorney. The attorney is required to keep the information you provide confidential and is generally protected from being forced to disclose the information by the attorney-client privilege. In the end, the representation your attorney is able to provide will only be as good as the information and guidance you are able and willing to provide.

Legal Fees

You should not agree to be represented by an attorney until you have a clear understanding of how you will be billed for the attorney's services. Attorneys typically charge for their services in one of the following three different ways:

- **On a contingency basis**. Contingency fees are generally limited to personal injury cases or other matters where there is some expectation that the client will receive a financial award. When the attorney charges contingency fees, these fees, which are typically stated as a fixed percentage of the award, are contingent upon receipt of the award. However, regardless of whether the client receives the award or not, the client typically remains responsible for paying expenses of the claim such as depositions, filing fees and court reporter fees. An attorney is unlikely to charge contingency fees in preparing a succession plan.
- **On a fixed fee-per-service basis**. Some attorneys will charge a fixed fee for standard routine matters such as simple wills, deeds, the search of a real estate title, representation in a simple bankruptcy or drafting a basic contract.
- **On an hourly basis**. Attorneys charge an hourly rate for almost everything else. The amount your attorney charges per hour will be determined by a number of factors, including the extent of his or her experience in estate planning and the generally accepted hourly charges for legal services in your community. In many instances, an attorney will request that you pay a retainer fee up front against which the attorney will bill his or her time. When you are being charged an hourly rate, you should always ask your attorney to periodically provide you with a complete, itemized bill so you can understand all of the services rendered and expenses incurred on your behalf.

Thus, at your first meeting with your attorney, you should discuss how you will be billed. You should expect to either be given a written letter or statement outlining the fee structure or sign an agreement regarding both the services to be provided and the charges for those services with your attorney so that both of you have a clear understanding of what to expect. Make sure that you carefully read this document and fully understand it before you sign it. This agreement should cover not only the

attorney's hourly rates, but also any extra costs that are to be passed on to you, such as copy costs, conference room charges, delivery charges, etc. Some attorneys may be willing to provide you an estimate of the likely total costs of the services to be provided to you. You may be able to negotiate fees with your attorney, but if you are going to do so, you should do so at the beginning of your representation and you should make sure that the outcome of this negotiation is reflected in the letter or agreement the attorney provides to you.

Working with Your Attorney

The quality and cost of the legal services you receive will depend, in part, upon how well you work with your attorney and vice versa. And, as is the case with most relationships, good communication is the key to a successful relationship. You should ask your attorney about his or her preferred method of communication and try to communicate in that way. However, if you communicate by email, you should avoid using your email at work or forwarding emails from your attorney to others as doing so may jeopardize the attorney-client privilege that helps keep those communications confidential. You should also ask to be copied on all correspondence pertaining to you and you should promptly and carefully read all materials given to you by your attorney.

The way in which you interact with your attorney can also affect the cost of the legal services provided by your attorney. An attorney's stock in trade is his or her time and anything that you can do that saves the attorney time will save you money. The following are some tips for keeping your legal fees low:

- A more experienced attorney, such as a partner or senior associate in a law firm, is going to charge a higher hourly rate than a less experienced attorney, such as a junior associate in a law firm. However, the more experienced attorney will sometimes be cheaper in the long run since that experience may enable the attorney to resolve your matter in less time than an attorney with less experience could.
- Attorneys typically bill for time spent on telephone calls with clients, so be smart and efficient when calling your attorney. Thus, you should refrain from asking the attorney questions that can be answered by a member of his or her staff. Also, attorneys typically bill in minimum increments of time ranging from one-tenth of an hour (i.e., 6 minutes) to one-quarter of an hour (i.e., 15 minutes). So, if you call your attorney to ask a question that they can answer in one or two minutes, you will often be billed the minimum increment of 6 to 15 minutes of time. As a result, you should always try to be prepared and organized when you

talk to your attorney and, if possible, wait to call your attorney until you have several matters to discuss.

- Plan meetings at your attorney's office to avoid being billed for travel time and costs.
- Make copies of documents before going to your attorney's office to save time and avoid copy costs.
- Use attorneys for legal matters and other professionals for other matters. Your attorney is an expert in the law. Your attorney is probably not the best person to be talking to about business strategy or financial or personal matters. Not only will the hourly rate charged by your attorney will be the same whether you are discussing legal or other matters, it will also likely be higher than the charges you would incur by consulting with other professionals about these other matters.
- Examine the itemized bill your attorney provides you for clues as to how effectively you are utilizing your attorney's time.

As a general rule, you should not take actions that will affect your succession plan without first consulting with your attorney. Something that might seem trivial or unimportant to you could have implications that you do not realize.

If you cannot make a scheduled appointment with your attorney, you should call as soon as possible to allow your attorney to devote that time to something else. You should avoid dropping by without an appointment, as your attorney will often have other appointments or deadlines to meet.

While you have hired your attorney and he or she certainly works for you, you must understand that attorneys are often involved in other matters that can prevent them from promptly responding to you or being able to work on your plan, particularly on short notice. On the other hand, while it is true that attorneys are often very busy, you have a right to know what work has been done for you and what activity is currently taking place on your behalf. Itemized bills and copies of correspondence should give you at least a fair or idea of how your matters are proceeding. If you become concerned about the extent of activity on your behalf, you should contact your attorney to get an update on where things stand. If your attorney is not able to provide you an update within a reasonable amount of time or you feel like your attorney is not adequately representing you, you can file a complaint with the Tennessee Board of Professional Responsibility (800-486-5714 or www.tbpr.org).

Conclusion

It is important to get the professional assistance you need in preparing your succession plan. While you will probably need the services of an attorney, you may also need the services of other professionals, such as an accountant, financial planner, bank or loan officer, insurance agent or family counselor. In acquiring these services, you should strive to be as sophisticated and knowledgeable a consumer as you can be. To a very large extent, this workbook is designed to help you achieve that goal.

After you identify which legal services are necessary, the next step is to find and choose the professionals who can provide those services. Given the importance of legal services to a succession plan, this chapter is focused on acquiring legal services. Finding an attorney to provide these services is relatively easy. However, finding an attorney that you can be sure is competent to provide the best service and who is right for you may require effort and careful thought. Even so, there are a number of ways to learn about attorneys before you hire one. It is important that you use these to find out as much as you can before you make the decision to hire an attorney.

Finally, the quality and usefulness of the professional services you receive will depend to a large extent on the relationship you have with the professional(s) providing these services. In general, the more clearly you are able to communicate your desires and expectations, the more likely you are to get the services you want and need. Similarly, the better you understand the process and the constraints you and your professional(s) face, the more likely you are to be satisfied with the services you receive.

A "Sample Attorney Estate Planning Questionnaire" is included in the appendix for Chapter 6 of this workbook. This form provides a sample of the type of information an attorney will need to begin the process of writing your will and developing your estate plan. Your attorney may require additional information depending on the complexity of the estate.

Chapter 7: Retirement Planning: Realities & Resources

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Get an Early Start

A lot of thinking and planning is necessary for funding your retirement years. The very best retirement planning is done very early in your working life. Always, when you're dealing with financial matters, your options are much better if you have time on your side. Setting aside enough for financial security is more important than ever because today's retirees are living longer than ever.

Retirement Income Sources: The Big Three

There are three basic sources of retirement income. You may have all three or a combination, depending on the nature and duration of your employment.

Social Security

The first and most common income source, Social Security, is designed to replace around 30 percent of your pre-retirement income for those with low to moderate earnings. Although in the past, households often looked to Social Security as their primary source of income for retirement, Social Security was never designed to completely fund retirement.

Employee-Sponsored Retirement Plan

If either you or your spouse is not self-employed, the second source of income is generally funded jointly by you and your employer. It may include pension funds or monthly annuity payments from one or more employer retirement plans. As an employee in your own farm or non-farm business, you also have options for funding your retirement through Simplified Employee Pension (SEP) or Savings Incentive Match Plan for Employees (SIMPLE) plans.

Farm or Business Transfer: An Important Decision. Make It Early!!

If you own a farm or business, you'll have two options, and each of these has very different implications for your retirement planning. If you want to pass your farm down intact to your heirs, it will be very important to protect your farm assets by setting aside enough personal (non-farm) assets to see you through your retirement years, and by making sure that you have enough long-term care insurance to finance end-of-life care. If you do not plan to pass your farm or business intact to your heirs, you'll be able to liquidate your farm or business assets to fund your retirement needs. Regardless of the option you choose, the earlier you make that decision and begin retirement planning, the better!

Personal Assets

Your third source is the personal assets you've accumulated throughout your working years. These could include savings and investments as well as personal and real property (land, timber, buildings, equipment, vehicles). Personal and real property will have to be liquidated to serve as a source of income, so once that has happened, the assets will not be available to pass on to your heirs. (See notes in Farm or Business Transfer Box.)

Retirement Planning

While planning for retirement may seem overwhelming, don't let that be an excuse for delaying those important decisions. The longer you delay, the fewer options you'll have. This section contains very basic information and resources for planning to help you get started. If your finances are complex – and particularly if you own a successful business – you'll need to also talk with a qualified financial advisor.

Basic Questions to Guide You

Your goal for successful retirement planning is not to have to drastically lower your level of living after retirement. Some key questions you'll need to ask are:

At what age do I plan to retire?

Retirement before age 65 has been an increasing trend in recent years, but the downside is that early retirees have fewer years to save, fewer years for their savings to grow and a longer time period to sustain themselves on invested assets.

How many years will I spend in retirement?

In the last century (1900 to 2000), average life expectancy increased by about 30 years. Many people are living into their 80s and 90s. The average worker now spends more

than 20 years in retirement – double the amount of time spent by the previous generation of retirees.

What income will I have from a retirement plan or Social Security?

If you or your spouse has worked outside your own farm or business, if you have paid enough Self Employment Tax or if you have made contributions on your own behalf to a SEP or SIMPLE Retirement Plan, you should have a regular income stream from one or more of these sources. Those funds can serve as a basis for your retirement needs.

How much will I have in personal assets?

You can draw on these funds or assets for special needs or even for day-to-day expenses if your necessities exceed your combined income from Social Security and your retirement plans.

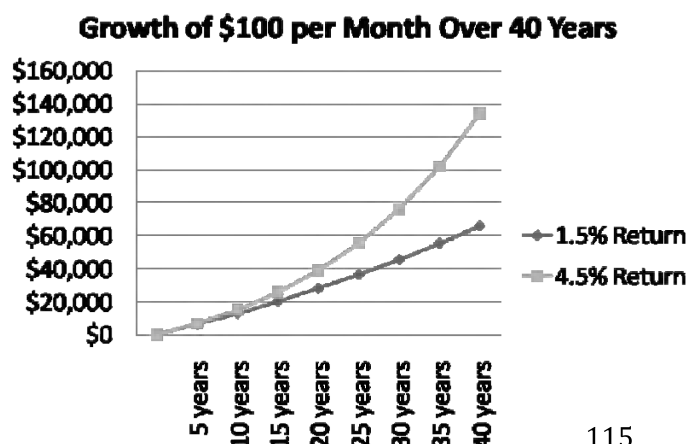
Estimating Retirement Needs

Retirement worksheets and calculators can help you plan more accurately for retirement. The American Savings Education Council's *Ballpark Estimate* worksheet is an easy way to get a general idea of the amount you need to save. You can access this online at http://www.choosetosave.org/ballpark/index.cfm?fa=interactive.

To complete a realistic retirement savings analysis, you need to know how much you'll receive from Social Security and/or an employer pension plan. Each year, the Social Security Administration (SSA) sends workers age 25 or older a benefit estimate statement that shows what they'll receive at ages 62, 65 and 70, in today's dollars, based on prior earnings. Statements are sent about three months before your birthday. You can also request a Social Security benefit estimate by calling 1-800-772-1213 or going online at http://www.ssa.gov.

Be sure to include pensions from all jobs in which you have vested benefits, even if you no longer work there, in your retirement projections.

Figure 7.1



Saving vs. Investing

We often talk about saving and investing as if they are interchangeable. However, there are two important distinctions. Savings accounts generally have a lower interest rate, but your money is safe

from market and/or interest fluctuations. Investments usually have a higher rate of return over time, but rates often fluctuate in the short term and your investment could even lose money.

For example, Figure 1 shows the growth of a $100-a-month contribution at two different rates of return – 1.5 percent and 4.5 percent. Your bank or credit union has safe savings options – savings or money market accounts – currently (2010) earning around 1.5 percent. At the end of 40 years– approximately your entire working career – your contributions would have earned interest in the amount of $17,715, for a final balance of $65,715. On the other hand, if you were able to earn a 4.5 percent return by investing in an option such as a mutual fund or a long-term bond fund, you would have earned $86,115 on your contributions, for a final balance of $134,115. Of course, with these rates, you may forfeit the safety of having your investments guaranteed by the government.

Investment Options

You do not need a sophisticated knowledge of investing to plan for your retirement. However, at minimum, you will need to know enough about basic investing to make intelligent decisions about the mutual fund options offered in 401(k)s or other retirement accounts. Ask your fund representative to fully explain the options available to you and the advantages and disadvantages of each.

When thinking about investment options, it's helpful to categorize them according to whether they are offered through the workplace or obtained on your own. The chart below lists common investment options in each category.

Workplace-sponsored	Personal
401(k) Retirement Plan	Individual Retirement Account (IRA)
401(k) Roth Retirement Plan	Roth IRA
403(b) Retirement Plan	529 Education Savings Plan
459 Retirement Plan	Coverdell Educational Savings Plan
SEP Retirement Plan	U.S. Treasuries
SIMPLE Retirement Plan	Mutual Funds
Keogh Retirement Plan	Brokerage Accounts (for stocks, bonds or other securities)
	Whole Life Insurance
	Annuities

Tax Considerations

Because the U.S. government wants to encourage its citizens to save for retirement, you can realize certain tax advantages on the money you put into retirement accounts that are not available in other accounts. For example, you can set some of your income aside in an Individual Retirement Account (IRA) or a 401(k) and defer paying taxes on that income until it is withdrawn at an eligible age. You may also put some of the money you've already paid taxes on in a Roth IRA or a Roth 401(k) and pay no taxes on the money it earns in the future. In the case of a Roth, both your contribution as well as all of the interest or return on your investment can be withdrawn tax-free after retirement.

Education savings plans, both 529 and Coverdell accounts, work in a similar way. They are financed with after-tax income but earnings grow tax free. In the case of the college savings plans, it is enrollment of the beneficiary in a qualified educational institution that triggers penalty-free withdrawal.

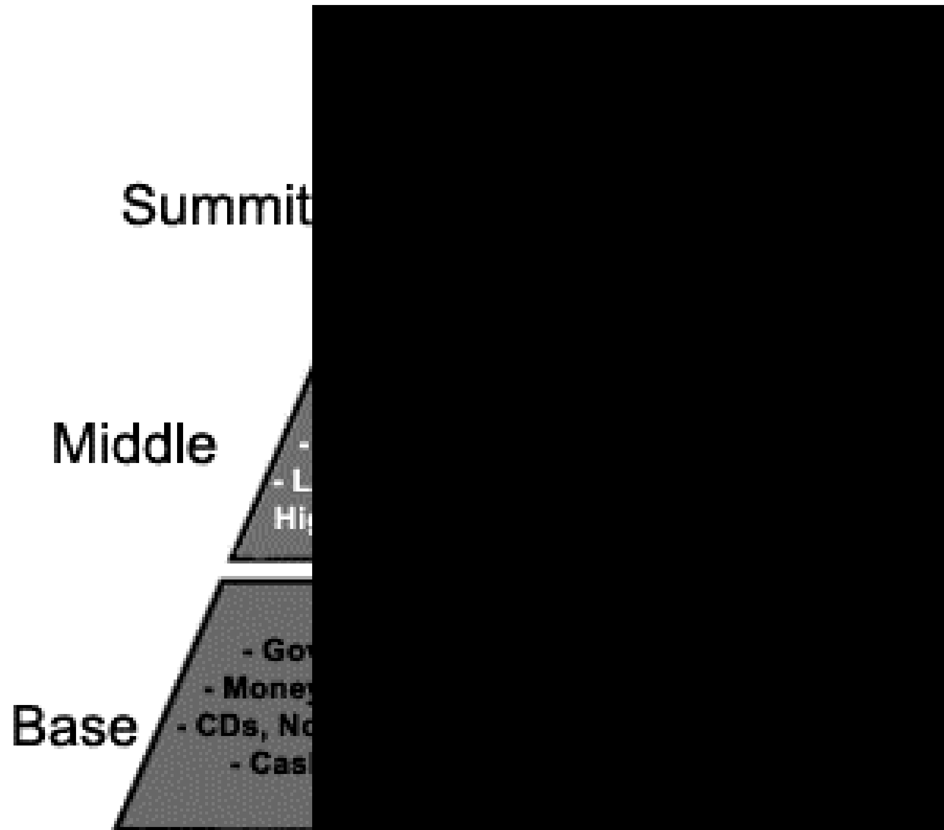
In all tax-deferred or sheltered accounts, whether they are retirement accounts or educational savings accounts, you will incur a heavy penalty for early withdrawal. If you take money out of a tax-sheltered or tax-deferred fund before you reach retirement, you'll pay a 10 percent penalty in addition to any taxes owed on the amount you withdraw. It's important to plan carefully before you commit funds to a retirement account, because that money won't be available for meeting the financial goals you have before you retire.

Tax-Deferred vs. Tax-Sheltered

In a tax-deferred account, you contribute money that has not yet been taxed. In reality, you are putting off (deferring) paying the tax on that money until after it is withdrawn from the account. Upon withdrawal, you'll pay taxes on both the amount you've contributed and what has been earned in interest or return. The assumption is that upon retirement you will be in a lower tax bracket and the money withdrawn will be taxed at a lower rate. In a tax-sheltered account, you contribute money on which you've already paid taxes. Your investment then grows tax-free, and when you withdraw funds at an eligible age or for an eligible reason, you pay no taxes on either your contributions or your earnings.

Risk vs. Return

In general, investments that yield a higher rate of return are the most risky, and investments with lower rates of return are usually less risky. You'll want your initial investments – those you depend on for meeting essential needs – in relatively safe investments. As you accumulate more and more money to invest, you can afford to invest in more aggressive – and risky – funds that provide you the opportunity to realize higher returns.



Most of us never reach the summit of financial security where we can afford to take the risks associated with individual speculative stocks, options, futures contracts and collectibles, but if your middle level investments turn out to be very successful, there's always that possibility!

How much risk should you take with your investments? Financial experts will say that the answer depends on two factors. The first is your *capacity for risk*. Your capacity for risk depends on the amount of your total assets. If you have more money than you need to be financially secure, you can certainly afford to take more risk than the person who

has just enough. Your capacity also depends on your financial responsibilities. If you have most of your money tied up in a business on which your income, and that of others, depends, you wouldn't have many funds available for speculative investments. Finally, your capacity for risk depends on your stage in life. If you are 25, you have many years to recover from investment losses before you are dependent on your investment income for day-to-day living. If you're 65, you don't have much time to recover from losses.

The second factor determining how much risk you should take is your personal *risk tolerance*. Some people are just more comfortable taking risks than others, while others prefer a more conservative approach to investing across the life cycle. You can answer some questions to determine your tolerance for risk using the assessment by completing Worksheet 7.1 in the appendix.

Regardless of your risk tolerance, you should diversify your investments to maximize return and minimize risk. By diversification, we mean that you should invest in a variety of types of funds so that if some lose value, others might hold or gain value.

Asset Allocation

The way you choose to divide your investments among different funds to manage your risks and reach your financial goals is called "asset allocation." Your asset allocation will need to change with your life changes and changes in the larger economy.

Financial Goals

Over your life, your asset allocation will change as you save for and achieve your financial goals. For example, if you are planning to use a portion of your investment for down payment on a house, you might want that money in a very safe fund. If you don't plan an immediate withdrawal of funds to meet a financial goal, you can afford more risk.

Personal Circumstances

Your asset allocation will change with your personal circumstances as well. If your life is affected by illness, job loss, divorce or a natural disaster, you would likely need to move non-liquid assets to cash, and at least for a time, hold those assets in very safe investments. As you accumulate assets beyond those you'll need to fund your basic immediate and future needs, you can afford to allocate those assets to riskier investments with the prospects of higher yields.

Larger Economy

You'll certainly need to consider what the economy as a whole is doing, re-allocating your investment assets to safer investments during turbulent economic times and to investments with more earning potential when the overall economy is booming.

Age

One of the most important factors in your asset allocation may be your age, or the number of years you plan to work before you retire. This is because time is on your side as a young investor. Since the larger economy and financial markets in general fluctuate and cycle, there are usually times when just about everyone makes money through investments and other times when just about everyone loses money. If you happen to lose money because of an economic downturn – which more severely affects riskier investments – when you are near retirement, you may not be able to leave your investments intact until the markets go back up. You may need to withdraw funds to supplement your retirement. If more of your funds are in safer investments – those not as vulnerable to economic fluctuations – as you near retirement, you don't face this risk.

Investment Costs

Costs associated with investing vary according to the type of investment and how they are purchased. You should try to minimize the costs as much as possible while still choosing your best options.

Cost Associated with Stocks

If you purchase stocks, you will pay fees to the broker who handles that transaction. Of course, you want to find the broker who charges the lowest fees. But often, brokers who discount their fees aren't available for us to ask questions and rely on them for support. If you are new to stocks and want the ability to pick up the phone and talk to your broker, you may want to pay more in fees for that support. If you are more comfortable investing, you may choose a discount broker.

Costs Associated with Mutual Funds

A percentage of a mutual fund investment that is deducted to cover the cost of managing the fund is called a **load**. Funds with a **front-end load** deduct the cost when shares of the fund are purchased. Funds with a **back-end load** make the deduction when the shares are sold. In a 401(k), the cost may be called a "fee" and will be listed in the fund report.

The Web site below contains a mutual fund expense analyzer. You can use this interactive online calculator to estimate the expenses of a fund that you are interested

in and to compare the potential expenses among funds. That can help you to decide which options are best for you.
http://apps.nasd.com/investor_information/ea/nasd/mfetf.aspx

In Closing

When you are investing, you should decide how active you want to be in making decisions about your accounts. If you choose to be active, you will need to watch your accounts carefully and move money between accounts and investment options to maximize your returns. If you remain passive, you will need to invest your money for the long term, essentially letting it ride the economic roller coaster over time.

Remember to fully investigate all your options before you invest. Consider whether your money is more appropriately invested in retirement or pre-retirement funds, what tax advantages you might realize from your choices, how safe your money is, whether it's in the best fund for your life circumstances and economic environment, the costs involved and how actively your investment must be monitored and managed.

What Do the Letters Mean?

Though credentialing for financial planners is not required by federal or state law, you should expect that persons calling themselves professionals to have the appropriate educational background, have significant professional experience, be licensed by the appropriate government regulatory agency, and have a commitment to helping others. A number of certifications and designations exist:

Certified Financial Planner (CFP) is probably the best-known certification in the field of financial planning. CFP licensees have to complete study and pass examinations in risk management, investments, tax planning, retirement planning and estate planning. They must also have a minimum level of three years work experience, continue to update their knowledge in the field, and adhere to a prescribed code of ethics. CFP licensees are certified by the Certified Financial Planner Board of Standards, Inc.

Chartered Financial Analyst (CFA) designations are awarded by the Association for Investment Management and Research (AIMR). Three levels of examinations can be taken. For example, the first level includes understanding investment analysis and management, financial markets, portfolio management and securities law.

Chartered Financial Consultants (ChFC) complete courses in economics, investments, insurance, taxation and related areas from the American College in Bryn Mawr, Pennsylvania.

Personal Financial Specialist (PFS) designations are obtained by some certified public accountants (CPAs). Additional specialized education is needed and other requirements established by the American Institute of CPAs must be met. CPAs with the PFS designation provide a broad range of personal financial services, which may include investment advice.

Accredited Financial Counselors (AFC) must pass two examinations, one in personal finance and one in financial counseling, and subscribe to the AFC code of ethics.

You can find out more about investment professionals and their qualifications by visiting the Web site below:

http://apps.finra.org/DataDirectory/1/prodesignations.aspx

Glossary

401k – an employer-sponsored retirement plan where contributions are tax sheltered and to which employers may make a matching contribution

529 – a college savings plan offered by state governments where contributions are tax deductible, withdrawals are tax free and the account is considered an asset of the donor

Active investing – a form of investing where the investor continuously monitors account activity, researches options, and buys and sells assets to increase his or her return

Annuity – a financial product purchased by an investor with a lump sum payment that pays the investor a series of payments at some point in the future

Asset allocation – the percentage of total capital invested in each major asset category, such as mutual funds, savings accounts or 401Ks

Balance sheet – a statement that provides an overall financial snapshot of the farm business by listing all of the business' assets (property) and liabilities (loans) and their respective values as of a specific date

Bonds – a debt investment in which an investor loans money to an entity (corporate or governmental) that borrows the funds for a defined period of time at a fixed interest rate

Broker – someone who charges a fee or commission to buy or sell an investment on behalf of another

Business life cycle – the different stages through which most businesses pass, from establishment to growth to maturity and finally to decline

Business plan – a written document that defines a business' product concept, potential customers and necessary financial resources needed to achieve the objectives of the business

Certificates of Deposit (CD) – a savings certificate with a fixed interest rate and maturity date, insured by the federal government

Certified financial planner – a financial professional paid for advice and planning who has passed a series of exams and met other requirements

Certified public accountant (CPA) – a financial professional paid for accounting and tax related functions

Closely held corporation – a corporation where most of the shares of stock are owned by a family or small group of investors and the stock is not traded on a public exchange

Collateral – assets pledged by a borrower to secure a loan or other credit, and subject to seizure in the event of default on the loan

College savings plan – one of several options that allow you to invest money to pay for an individual's college education

Common stock – a security that evidences proportionate ownership or equity capital of a corporation and gives its holder a claim on the corporation's assets and income (after corporate obligations are paid)

Conservator – one who is appointed by a court to manage the estate of one who is unable to effectively manage his or her business and property affairs

Contract – an agreement between two or more parties consisting of a promise or a set of promises that are enforceable by law

Cooperative – an enterprise or organization owned by and operated for the benefit of those using its services

Corporation – a business structure that is recognized as an entity that is separate and distinct from its owners and where the entity earns the profits and assumes the liability of the business

Coverdell – a type of college savings plan where contributions are not tax-deductible but withdrawals are tax-free and the account is considered to be an asset of the student

Current assets – assets that are readily convertible into cash, usually within one year, without loss in value

Current liabilities – the amount owed for interest, accounts payable, short-term loans, expenses incurred but unpaid, and other debts due within one year

Debt capital – the assets of a business that are financed with loans evidenced by promissory notes, bonds or debentures.

Deed of trust – a document that grants a lender an interest in real property to secure repayment of a loan by a borrower

Diversification – dividing the money you invest among a variety of options so that your overall risk of losing money is lowered

Equity capital – the assets of a business acquired through the transfer of ownership in the business. For corporations, equity capital is raised through the sale of stock.

Estate planning – the preparation of a plan of administration and disposition of one's property before or after death

Estate tax – a tax imposed by either the federal or a state government on the right to transfer property at death

Executor – a person named in a will to administer the estate

Farm operator – the person who runs the farm, making the day-to-day management decisions. The operator could be an owner, hired manager, cash tenant, share tenant and/or a partner. If land is rented or worked on shares, the tenant or renter is the operator.

Fees – money charged for financial transactions

Financing statement – a brief document describing the **collateral** that is being used to secure a loan and providing the names and addresses of both lender and borrower that are filed as a public record to give third parties notice of the lender's interest in the **collateral** and establish the lender's interest relative to other parties

General partner – an owner and operator of a partnership, who is personally liable for all the debts of the partnership

General partnership – a voluntary association of two or more persons formed for the purpose of operating, as co-owners, a business for profit

Income statement – a document that lists all expenses, income and changes in inventory for a business during a specific period of time

Interest rate – a percentage of the money you save or borrow that represents the annual cost of credit

Intermediate assets – assets with a useful life of one to 10 years, they usually support production and are not sold or converted into cash on an annual basis, including machinery, equipment and breeding livestock

Intermediate liabilities – debts with a term of one to 10 years. The value given as intermediate liabilities on the balance sheet should reflect the balance remaining after the coming year's principal and interest have been paid.

Investing – the act of purchasing a financial product or other item of value with the expectation of earning a favorable return on the amount of money paid for the item

Individual retirement account (IRA) – a retirement account where contributions are tax-deductible and distributions are taxed at applicable marginal tax rates at time of withdrawals. Penalties for withdrawal before age 59½ apply.

Joint and several liability – a type of shared liability where the creditor may sue and collect the entire liability from any one or more of the liable parties or all of the liable parties together, at the option of the creditor. The liability of general partners in a partnership for partnership obligations is joint and several.

Joint tenancy – a form of co-ownership of real or personal property where the co-owners have the **right of survivorship.** Title to the property remains with the surviving co-owners upon the death of one of the co-owners and so on to the last survivor.

Joint venture – an association of two or more parties to conduct a single or isolated project with a limited duration for mutual profit

Keogh retirement plan - a tax-deferred qualified retirement plan available to self-employed people and unincorporated businesses

Liability – the legal responsibility for a loss or injury

Life cycle – the normal stages through which an individual passes over time

Limited liability company ("LLC") – a form of business organization that has the attributes of both a partnership and a corporation, as it is characterized by limited liability, management by a member or members, and limitations on the transferability of ownership interests.

Limited liability partnership ("LLP") – a special form of partnership where an individual partner does not have liability for another partner's misconduct or negligence

Limited partner – a partner in a limited partnership who has no management authority and whose liability is limited to the amount of his or her investment

Limited partnership – special form of partnership that has both general and limited partners

Liquidity – the ability to convert an asset to cash quickly and without loss of value

Long-term – a time range composed of a period of years as opposed to days, weeks or months

Long-term assets –assets with a useful lives of more than 10 years that usually cannot be easily sold without disrupting the business. Long-term assets include land, timber, buildings and improvements.

Long-term liabilities – debts with a term greater than 10 years, generally representing debt of a long-term asset

Money market account – a type of short term savings that allows limited withdrawals and check writing

Mortgage – see **Deed of Trust**

Mutual funds – Accounts where several investors pool their money to buy a variety of investment options, resulting in increased diversity and reduced risk

Net worth – the total value of a company's assets minus the total value of the company's liabilities on a given date

New generation cooperative – a relatively new type of cooperative used primarily in the value-added processing of agricultural commodities

Pass-through entity – a legal entity that is not taxed, where profits and losses "pass through" the entity to its investors or owners who report the entity's profits or losses on their individual tax returns

Personal property – all property other than real property

Preferred stock – a type of corporate stock that provides a specific dividend that is paid before any dividends are paid to common stock holders, and which takes precedence over common stock in the event of a liquidation of the corporation

Probate – court proceedings pertaining to the administration of an estate

Promissory note – a promise to pay an amount or amounts at a specified time. Promissory notes evidence debt.

Public or publicly traded corporation – corporation with many shareholders that is traded on a national stock exchange

Real property – land and items attached to or erected or growing upon land including timber

Return – the money received for saving or investing, usually stated as a percentage of the amount originally contributed

Right of survivorship – the right of a surviving co-owner to a deceased's interest in property

Risk – the chance that an investment's actual return will be lower than expected, including the possibility of losing the original money invested

Risk capacity – the financial ability to assume risk and possibly lose part or all of an investment

Risk tolerance – the emotional ability to assume risk and take the chance of losing all or part of the original investment

Roth 401k – a type of 401k where employee contributions are not tax-sheltered (made with after-tax dollars) but distributions from the employee portion of the fund are tax-free after retirement

Roth IRA – a type of IRA where contributions are not tax-deductible but distributions after retirement are tax-free

S corporation (or subchapter S corporation) – a corporation for which the shareholders have elected to have the corporation treated as a **pass-through entity** where the corporation's profits are taxed to the shareholders at individual income tax rates

Saving – setting aside money in an easily accessible short-term account

Savings account – an account that provides total access to the money deposited in the account and pays a relatively low interest rate

Savings Incentive Match Plans for Employees of Small Employers (SIMPLE) - A retirement plan sponsored by companies with fewer than 100 employees, which is attractive for employers because it avoids some of the administrative fees and paperwork of plans such as a 401(k) plan. A SIMPLE plan may be structured as either a 401(k) or an IRA.

Securities – an investment instrument, other than an insurance policy or fixed annuity, issued by a corporation, government or other organization, which offers evidence of debt (a loan) or equity (ownership), such as stocks, bonds, mutual funds

Security agreement – a written agreement between a borrower and a lender that gives the lender an interest in the **collateral** being used to secure the debt. The security agreement secures the debt and establishes rights between the lender and borrower relative to the **collateral**.

Security interest – lender's right to take **collateral** for a loan if the borrower defaults on the promissory note or other loan documents

Shareholder – an owner of shares of stock in a corporation

Simplified Employee Pension (SEP) - A retirement program for self-employed people or owners of companies with fewer than 25 employees, allowing them to defer taxes on investments intended for retirement. This type of plan allows employers to contribute on behalf of eligible employees, and all such contributions are tax-deductible as a business expense.

Sole proprietor – the owner of a sole proprietorship

Sole proprietorship – a business run by a single owner who owns the business, earns all profits and is completely responsible for any business debt or other obligations. In a business run as a sole proprietorship, there is no legal distinction between the business and the individual.

Stock – transferable certificates that represent ownership in a corporation, which can be bought and sold

Stockholder – see **Shareholder**.

Succession planning – the process where management, income and ownership of a family business' assets are transferred to a succeeding operator

Tax-sheltered – an investment that is at least partially free from taxation

Tenancy by the entirety – a **joint tenancy** between spouses that becomes a tenancy in common in the event of divorce

Tenancy in common – a form or co-ownership of property where the co-owners have no right to each other's interest upon the death of the other (compare to **joint tenancy**).

Treasury bill – an investment option offered by the government that is sold in $1,000 increments with due dates of less than one year from the date of sale.

Trust – a legal entity created through a trust document in which the creator or trustor places assets to be managed by a named "trustee" for the benefit of the "beneficiaries" of the trust

Trustee – the person or institution named in a trust to oversee and manage the assets in the trust according to the terms of the trust

Trustor – the person who creates a trust and places assets into a trust, also referred to as the grantor or settlor

Will – a legal document lists instructions regarding the distribution and management of your assets or property after your death.

Withdrawal – the removal of funds from a savings or investment account

Additional Resources

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Chapter 7: Retirement Planning

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WORKSHEET 2.1: Rating Lifestyle Values and Choices

Adapted from Farm Transfers in Wisconsin: A Guide for Farmers, Wisconsin Dept. of Agriculture

Directions: Please rate the importance (to you personally) of each item listed below [**with 1 = not important and 5 = extremely important**]. Have each family member complete the survey to help get a clearer picture of what is most important to each person in the farm transfer process. Then discuss each item with all parties involved in the farm succession planning process.

1.	I want the farm to remain in our family's possession.	1	2	3	4	5
2.	I want the farm to continue to be farmed after I/we retire.	1	2	3	4	5
3.	I want to keep physically involved in the business after I retire.	1	2	3	4	5
4.	I would like to see my children play a part in the continuation of the farm.	1	2	3	4	5
5.	I would like the division of farm property among our children to be equal in dollar value.	1	2	3	4	5
6.	I want the division of farm property among our children to be fair (not necessarily equal).	1	2	3	4	5
7.	It's important that my spouse and I agree on the plans for transfer of the farm.	1	2	3	4	5
8.	It's important that my spouse and I have enough money for retirement.	1	2	3	4	5
9.	I want to have the financial resources to do new things after farming.	1	2	3	4	5
10.	It's important that our children agree with our plans for the farm's future.	1	2	3	4	5
11.	I want to help our children establish themselves in careers outside farming.	1	2	3	4	5
12.	I want to be able to give financial help to our children who choose a non-farm career.	1	2	3	4	5

13.	I want to be able to give financial help to our children who choose a farm career.	1	2	3	4	5
14.	I would like to maintain some financial control over the farm throughout my life.	1	2	3	4	5
15.	I would like to be involved in decision making for the farm throughout my life.	1	2	3	4	5
16.	I would like our children to play a part in the decision making for the farm's future.	1	2	3	4	5
17.	I would like our children to assist in my/our plans for retirement.	1	2	3	4	5
18.	I want to receive what our farm is worth when it is transferred.	1	2	3	4	5
19.	It's important to me that our children take over the management of the farm.	1	2	3	4	5
20.	It's important to me that our children choose farming as a career.	1	2	3	4	5
21.	It's important to me that our children have the opportunity to choose a career outside farming.	1	2	3	4	5
22.	I want our children to have the opportunity to continue the operation of the family farm.	1	2	3	4	5
23.	I would like everyone in the family to be satisfied with the way the farm/estate is handled.	1	2	3	4	5
24.	It's important to me that our children's requests regarding the farm transfer be honored.	1	2	3	4	5
25.	I would sell the farm if the price was fair.	1	2	3	4	5

You can download this worksheet at: http://www.farmlandlegacy.org/

WORKSHEET 2.2: Rating Your Comfort Level

Adapted from Planning the Future of Your Farm by North Carolina Farm Transition Network

Directions: 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 1 to 5 [**with 1 = very uncomfortable and 5 = extremely comfortable**]. Then discuss each item with all parties involved in the farm succession planning process.

Possible Actions	Very Uncomfortable				Extremely Comfortable
Expanding the size of the operation	1	2	3	4	5
Reducing the size of the operation	1	2	3	4	5
Taking on large amount of added debt	1	2	3	4	5
Adding new enterprises	1	2	3	4	5
Eliminating one or more enterprises	1	2	3	4	5
Making dramatic changes to the operation	1	2	3	4	5
Taking more time away from the operation	1	2	3	4	5
Increasing the amount of physical labor you provide to the operation	1	2	3	4	5
Increasing your managerial responsibilities	1	2	3	4	5
Relinquishing managerial responsibilities	1	2	3	4	5
Working with a new managerial partner	1	2	3	4	5

Comments from discussion:

You can download this worksheet at: http://www.farmlandlegacy.org/

WORKSHEET 2.3: Goal Setting/Action Planning

Directions: After the group discussion of individual wants and needs possibly using Worksheets 2.1 and 2.2. List the goals that were agreed upon below and fill in the corresponding objectives, action steps, person (s) responsible and deadline.

Goal	Objectives	Action Steps	Person (s) Responsible	Deadline
1)				
2)				

You can download this worksheet at: http://www.farmlandlegacy.org/

WORKSHEET 3.1 - Balance Sheet

Name:
Date:

Assets

CURRENT FARM ASSETS	Value
Cash and checking balance	
Total cash and checking	
Prepaid expenses and supplies	
Total prepaid expenses and supplies	
Growing crops	

Total growing crops	
Accounts receivable	
Total accounts receivable	
Hedging accounts	

Total hedging accounts			
Other current assets			
Total other current assets			
Crops on hand	Quantity	Value per unit	
Total crops on hand			

Crops under government loan							
Crop	Quantity	Loan rate	Interest rate	Month entered	Year entered	Value per unit	Value
Total crops under government loan							

Market livestock	Number	Avg. weight	Value per unit	
Total market livestock				
Total current farm assets (sum of categories above)				

INTERMEDIATE FARM ASSETS				
Breeding livestock	Number	Value per head	Cost value	Market value

Farm machinery & equipment				
Titled vehicles				
Other intermediate assets				
Total intermediate farm assets				
LONG-TERM FARM ASSETS				
Farm land	Acres	Value per acre	Cost value	Market value
Farm buildings				
Other long-term assets				
Total long-term assets				

TOTAL FARM ASSETS (sum of current, intermediate and long-term assets)		
Schedule P: Nonfarm assets	Cost	Market
Savings and checking		
Stocks and bonds		
Other current assets		
Household furnishings and appliances		
Nonfarm vehicles		
Cash value of life insurance		
Retirement accounts and IRAs		
Other intermediate assets		
Nonfarm real estate		
Other long-term assets		

TOTAL NONFARM ASSETS		
TOTAL ASSETS (Total farm assets + Total nonfarm assets)		

Liabilities

CURRENT FARM LIABILITIES	Amount
Accrued interest (sum below)	
Accounts payable and other accrued expenses	

Current loans	Interest rate	Principal balance	Accrued interest	P & I payment	Month due	Balance
Annual operating						
Government crop loans						
Principal due within 12 months on term loans (sum below)						
Total current farm liabilities						

INTERMEDIATE	Interest rate	Principal balance	Accrued interest	P & I payment	Month due	Final year	Principal due	Intermediate balance
Total intermediate farm liabilities								

LONG-	Intermediate	Principal	Accrued	P & I	Month	Final	Principal	Long Term

TERM	rate	balance	interest	payment	due	year	due	balance
Total long-term farm liabilities								
TOTAL FARM LIABILITIES								

NONFARM LIABILITIES	
Schedule V: Nonfarm liabilities	Amount
Nonfarm accrued interest (sum from below)	
Accounts payable and other accrued expenses	
Principal due within 12 months on term loans	

Loans	Interest rate	Principal balance	Accrued interest	P & I payment	Month due	Final year	Principal due	Balance

Current									
Intermediate									
Long-term									
Total nonfarm liabilities									

NET WORTH	Cost	Market
Total farm and nonfarm assets		
Total farm and nonfarm liabilities		
Deferred tax liabilities		
TOTAL LIABILITIES		
Retained earnings/Contributed capital (Total assets – Total liabilities) Cost basis only		
NET WORTH (Total assets – Total liabilities)		

Net Worth is calculated by subtracting Total Liabilities from Total Assets.

Rental and Lease Information

Land – Legal description	Landlord	Acres		Type of lease	Annual cash rent	Payment date(s)	Expiration date
		Total	Crop				
Other items – description	Owner	Number of units		Type of lease	Annual payment	Payment date(s)	Expiration date

WORKSHEET 3.2 Rate Your Records

Please answer “Yes” or “No” to the following questions.

____ 1. Will your records give you an electrocardiogram of your business?

____ 2. Do your records provide the basis for management decision making?

____ 3. Do you know from whom and how much is owed to you?

____ 4. Do you know to whom and how much you owe?

____ 5. Are your records complete enough to convince an IRS auditor your tax return is accurate?

____ 6. Do your records satisfy your lender’s requirements?

____ 7. Do you have records of all loans received and loan payments made?

____ 8. Are you using recognized accounting principles and components?

____ 9. Does it take longer than 60 seconds to find something in your filing system, and can your spouse find it in 60 seconds or less?

____ 10. Does your record system maintain a complete and accurate accounting of receipts and expenditures?

____ 11. Can you determine your financial position from your records?

____ 12. Can you develop a cash flow statement based on information from your records?

____ 13. Can you accurately analyze and plan your farming operations based on information from your records?

____ 14. Are inventories maintained accurately and completely?

____ 15. Are complete and accurate cropping and livestock records kept?

____ 16. Do you input or record the data in your records on a regular basis?

____ 17. Do you file records and documents from past years?

____ 18. Is your checking account accurate and up-to-date?

____ 19. Are your records on farm family living expenses accurate?

____ 20. Is your office well-organized, well-equipped and pleasant to work in?

Count the number of questions with a “Yes” answer. Use the following rating system to determine how well-organized your record keeping system is.

20 – Very efficient
15 - 19 – Good job. Work on those critical areas.
8 - 14 – Good start but you have some weak points. “Even if you are on the right track, you will get run over if you just sit there.” - Will Rogers
7 or less – You need to make improvement a priority. You probably need to upgrade the shoe box.
Adapted from Pennsylvania Farm Bureau - Farm Management Services

WORKSHEET 3.3 Record of Important Papers

You have many important papers relating to personal records, property ownership, insurance, finances and other business affairs. This guide will help you inventory your important papers, locate papers when needed, direct others in an emergency and evaluate your family business affairs. Fill in this publication and keep it at home. Review it at least once a year. Bring it up to date whenever a significant change occurs. You may wish to prepare a copy for a relative or close friend for use in an emergency.

Information adapted from:
Oregon State University Extension Service
University of Florida – IFAS Extension
University of Tennessee Extension
Utah State University Cooperative Extension

Family Record

List all family members including children married and or living away from home. Under **comments**, include such information as health conditions, membership in organizations, etc. that would be useful in an emergency.

Name	Date of Birth	Where Birth Recorded and Location of Birth Certificate	Social Security Number and Location of Card	Comments

Close Relatives or Friends

List those persons who should be notified when serious emergencies occur.

Name	Relationship	Address & Phone Number

Personal Information

List any personal information including marriage certificates, death certificates, divorce decrees, military service, passports and drivers licenses.

Record	Where Kept	Where Recorded	Date
Marriage Certificates			
Divorce Decrees			
Death Certificates			
Military Service Records			
Citizenship Papers			
Passports			
Drivers Licenses			

Health Records (name)________________________________

Record health information here. Use one sheet for each family member.

Date	Illness, Disease, Accident or Immunization	Doctor's Name and Address	Other Information

Important Advisers and Contacts

Write names and addresses of any advisers you depend on in your personal and business affairs.

Name	Address & Phone Number
Accountant	
Attorney	
Banker	
Other banker	
Other banker	
Business manager/Partner	
Childcare provider	
Childcare provider	
Children's school contacts	
Children's school contacts	
Children's school contacts	
Children's school contacts	
Clergy	
Doctor	
Other doctor	
Other doctor	
Other doctor	
Other doctor	
Other doctor	
Other doctor	
Dentist	
Employer	

Important Advisers and Contacts

Write names and addresses of any advisers you depend on in your personal and business affairs.

Name	Address & Phone Number
Executor of will	
Executor of will	
Financial counselor	
Financial planner	
Forester	
Guardian of children	
Guardian of children	
Insurance agent (other)	
Parents (maternal)	
Parents (paternal)	
Stockbroker	
Other	

Location of Your Important Papers

Being able to find your important papers quickly is important to you and your survivors. Under Location, clearly identify the specific desk and drawer, closet, box, etc.

Important Papers	Location	Important Papers	Location
Wills and Instructions		**Personal Property Papers**	
Husband's will		Checkbooks	
Wife's will		Savings passbooks and certificates	
Copies of will		Insurance (life, health, accident)	
Funeral directions – cremation, burial		Stock certificates	
Memorial society membership		Savings bonds	
Special letters of instruction		Safe deposit box and key	
Power of attorney		Income tax records	
		Canceled checks and stubs	
Personal Papers		Inventory of household goods	
Birth certificates		Automobile title	
Baptismal certificates		Registrations – auto, dog, etc.	
Marriage certificates		Guarantees on appliances	
Adoption certificates		Appliance instruction books	
Divorce decrees		Credit cards (list them)	
Naturalization papers			
Diplomas		**Real Estate Papers**	

Important Papers	Location	Important Papers	Location
Passports		Deed to your house	
Social Security cards		Deed to other real estate	
Employment records		Record of improvements	
Military service records		Mortgage papers	
Family health records		Mortgage payment receipts	
Management Plans		Insurance policies	
Business Plans			

Banking Services

This list can help you track the checking, savings and other types of accounts you have at financial institutions.

Name and Address of Financial Firm	Identification Number	In Whose Name(s)
Checking accounts		
Savings accounts		
Certificates of deposit		
Money market accounts		
Trust accounts		
Safe deposit box		
Other		

Cards (credit, debit, ATM, etc)

This list can help you track the cards you have, and would be extremely helpful to those who handle your affairs during serious illness or after your death.

Type	Card Name & Issuer Address	Account Number	In Whose Name

Real Estate and Business Interests

List real property and business interests owned by the family. Also include mortgages held. **Kind of ownership** refers to the legal form of ownership such as tenancy in common or joint tenancy.

Kind of Property	Location (address)	Name(s) of Owner(s)	Kind of Ownership	Date Acquired	Purchase Price
Residence(s)					
Business(es)					
Timeshares					
Cemetery plot(s)					
Timber					

Other Personal Property

List autos, boats, mobile homes and other items of value (jewelry, antiques, books, collections, royalties, patents, etc).

Name of Asset	Date Acquired	Purchase Price or Value	Other Useful Information (name of owner, vehicle ID no., appraisals, etc.)

Stocks, Bonds and Securities

List any United States savings bonds, treasury securities, government agency securities, corporate and governmental stock certificates, and other securities you own.

Name of Asset	Serial Number	Date Purchased	Purchase Price	Other Useful Information (name of owner, no. of shares, maturity date)

Mutual Funds

List any mutual funds and money-market funds you own.

Name of Asset	Serial Number	Date Purchased	Purchase Price	Other Useful Information (name of owner, no. of shares, maturity date)

Money Owed

This list can help you track the debt you have, and would be extremely helpful to those who handle your affairs during serious illness or after your death. (home, autos, home equity, furniture, appliances, etc)

Person or Company Owed	Address	Amount of Original Debt	Terms of Payment

Money Owed to Us

This list can help you track the money others owe you, and would be extremely helpful to those who handle your affairs during serious illness or after your death.

Person or Company	Address	Amount of Original Debt	Payment Amount and Date

Property Insurance

In this section, inventory your insurance policies.

Description of Property Insured	Kind of Risk Insured	Amount of Coverage	Policy Number	Name of Company
Real estate				
Automobiles				
Other personal property				
Personal liability				
Other				

Life Insurance and Annuities

Inventory all life insurance policies and annuities carried on members of the family. Indicate kind of policy such as term, whole life, endowment, family income, etc. If owner of policy is not the person insured, give both names.

Person Insured	Kind of Policy	Face Value	Policy Number	Beneficiary	Name of Company

Health Insurance – Accident, Disability, Hospital

Include health, major medical, other employers' insurance, Medicare, and/or individual policies on family members.

Person(s) Insured	Kind of Policy	Amount of Coverage	Policy Number	Name of Group or Company Providing Insurance

Power of Attorney

If you have given someone the written legal power to act for you in case you become unable to handle your own financial affairs, indicate below.

Name	Address & Phone Number

Wills

Include information regarding construction and location of wills.

Date of Latest Will	Name(s)	Executor	Attorney
			Address
			Phone Number

Membership in Organizations/Clubs

This list can help you track your memberships in church, civic, professional and other organizations.

Name of organization/club	Address & Phone	Membership Information	
		In whose name	Number

Social Security, Retirement and Employment

Information concerning these items is often needed in filing applications, checking records, settling estates, etc.

<table>
<tr><th colspan="2">Social Security</th><th colspan="3">Employment Record</th></tr>
<tr><th>Name of Insured</th><th>Social Security Number</th><th>Family Member</th><th>Dates of Employment</th><th>Name of Employer</th></tr>
<tr><td></td><td></td><td></td><td></td><td></td></tr>
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<tr><td></td><td></td><td></td><td></td><td></td></tr>
<tr><th colspan="2">Retirement, Pension, or Profit-Sharing Plan</th><td></td><td></td><td></td></tr>
<tr><th>Person in System</th><th>Name of System</th><td></td><td></td><td></td></tr>
<tr><td></td><td></td><td></td><td></td><td></td></tr>
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</table>

Guarantees and Warranties

This list can help you track the guarantees and warranties you have on different items. (appliances, jewelry, etc)

Item	Coverage & Expiration Date

Frequently Used Web sites, User Names and Passwords

Keeping up with user names and passwords can be difficult especially when they must change periodically. This list can help you keep track of frequently used Web sites such as internet banking, online statements and online purchasing accounts (Amazon, eBay, etc.).

Web site	User Name	Password

Household Inventory   Room: ______________________

This list can help you track the important items in your home. Make copies of this form and list inventory in each room separately. (A home video record can take the place of a written record as long as the information below is included.)

Article	Place & Date Purchased	Model & Serial Number	Cost

WORKSHEET 3.4 Items of Sentimental Value

Use the worksheet below to list important personal possessions, their meaning and potential recipients of the items.

Personal Possessions	Special Meaning	Potential Recipients

WORKSHEET 3.5 Family Living Monthly Cash Flow Plan

Use the worksheet below to assist you in accurately spending each dollar of income for the month by assigning a dollar amount to the correct category.

Item	Amount	Item	Amount
Giving/Donations		Medical/Health	
Saving		Disability Insurance	
Retirement Fund		Health Insurance	
Education Fund		Long-Term Care Insurance	
Housing		Medical Bills	
First Mortgage		Dentist	
Second Mortgage		Optometrist	
Rent		Medications	
Real Estate Taxes		Personal	
Homeowner's Insurance		Life Insurance	
Repairs		Child/Dependent Care	
Replace Furniture		Toiletries/Cosmetics/Hair Care	
Other-		Household Supplies	
Utilities (non-farm)		Education/Adult	
Electricity		School Tuition	
Water		School Supplies	
Gas		Child Support	
Phone		Alimony	
Trash		Subscriptions	
Cable		Organization Dues	
Food		Gifts & Holidays	

Item	Amount	Item	Amount
Transportation		Partnership Withdrawals	
Vehicle Payment		Corporate Dividends	
Vehicle Payment		Personal Debts	
Gas & Oil		Credit Card	
Repairs & Tires		Credit Card	
Car Insurance		Credit Card	
License & Taxes		Credit Card	
Car Replacement		Gas Card	
Clothing		Credit Line	
Personal Care		Student Loan	
Recreation		Other	
Entertainment		Other	
Vacation		Other	
Miscellaneous		Other	

WORKSHEET 3.6 Lump Sum Payment Planning

Some expenses shown below occur only once or twice a year. Use this worksheet to assist you in determining how much money should be set aside each month to save for the expense.

Item Needed	**Annual Amount**	**Monthly Amount** (divide annual amount by 12)
Real Estate Taxes		
Homeowner's Insurance		
Home Repairs		
Replace Furniture		
Medical Bills		
Health Insurance		
Life Insurance		
Disability Insurance		
Non-Farm Vehicle Insurance		
Non-Farm Vehicle Repair/Tags		
Replace Non-Farm Vehicle		
Clothing		
Tuition		
Bank Note		
IRS (Self-Employed)		
Vacation		
Gifts/Holidays		
Other-		
Other-		

WORKSHEET 3.7 Reminder of Special Expenses

Some expenditures occur only once or twice a year. For example, car insurance premiums, property taxes, expenses related to holidays, special events, vacations and expenses for seasonal activities (skiing and hunting). Use this worksheet to remind you when these occur and how much they cost.

January Total: ________________	**February** Total: ________________	**March** Total: ________________
April Total: ________________	**May** Total: ________________	**June** Total: ________________
July Total: ________________	**August** Total: ________________	**September** Total: ________________
October Total: ________________	**November** Total: ________________	**December** Total: ________________

WORKSHEET 4.1 Multi-Generational and Joint Business Operation Quiz

Personal relationships as well as business characteristics are important to the success of multi-generational businesses. Thus, before deciding to go into business with family or others, you should complete a comprehensive evaluation of the farm or family business resources. One part of this evaluation should focus on identifying the personal strengths and weaknesses of the team of individuals who are going to be involved in the management and operation of the business. More specifically, the following personal characteristics should be appraised before a partnership or other jointly owned and operated business is formed:

1. **Common or complementary objectives and goals**. Individual goals are likely to be different, especially if the individuals are in different generations. While goals may differ, it is important that these do not conflict with one another. If you cannot agree on common or complementary goals, don't farm or go into business together.
2. **Ability to work, learn, share ideas and manage together**. Working together effectively often requires a shared work ethic and plan. It also means sharing achievements, problems and ideas. Working and managing together requires communication, compromise and commitment. Each person should be willing to divide responsibility and accept decisions for which the other person is responsible. Each person must be willing to give and take without losing sight of common goals and objectives.
3. **Respect for your partner and confidence in ability and business arrangement**. Farm or go into business together if you and your partner have the personal characteristics that blend together and if you have a plan that you know will work. Completing the attached quiz will help you appraise your own qualifications for farming or going into business together.

Take the following test to help determine if you have the personal characteristics to successfully farm or go into business with a partner or co-owner/operator. Everyone planning to farm or go into business together should take Test A. If you are going to farm or go into business with family members, you should take either Test B or C in addition to Test A. Members of the senior generation should take Test B, while members of the junior generation should take Test C. In answering the questions for all three tests, use the following point scale:

Your Answer	Your Points
Yes! Yes! Yes!	10
Yes	8
Maybe Yes	6
Don't Know	4
Probably No	2
Very Unlikely	1
Definitely No!	0

Test A – For any and all parties to the potential agreement:

Question	Answer Pts
1. Do you prefer to work and plan together vs. work alone and plan independently?	______
2. Are you willing to talk things over and make joint management decisions vs. “do it your way”?	______
3. Are you willing to listen and accept ideas/suggestions from others with less experience, less training or less education?	______
4. Are you able to make suggestions and recommendations versus giving orders and believing “my way is best”?	______
5. Are you willing to give others credit for things well done and accept responsibility for failures?	______
6. Can you discuss business and family issues with your potential business partner without getting angry?	______
7. Do you prefer to figure out how to get things done more effectively versus “do it like you always have done it”?	______
8. Do you like to recruit, hire, train, supervise and evaluate employees?	______
9. Are you willing to monitor and analyze the farm business and financial records, production records and recommend changes based on your analysis?	______
10. Are you willing to arrange and attend a weekly meeting?	______
11. Are you willing to develop a written business agreement?	______
12. Are you willing to review the business agreement and update it when necessary?	______
Total Points	______

Test B – Additional questions for the senior generation

Question	Answer Pts
1. Are you ready to turn over specific management responsibilities to the younger generation and are you willing to encourage and help them develop their management expertise?	______
2. Do you have a feasible plan for transferring the ownership of the farm business to the junior generation? Are you willing to recognize their earned equity as part of this plan?	______
3. Are you willing to borrow additional capital to build up the business to support two generations?	______
4. Are you willing to accept a junior partner with a different living style? Can you let his/her family have their own life yet help them to get through family crises with praise, encouragement and care?	______
5. Are you willing to plan and hold a family conference to discuss goals, roles, differences and expectations? Are you ready to help; the younger generation identify their farming future and help them get there?	______
Total Points	______

Test C – Additional questions for the junior generation

Question

Question	Answer Pts
1. Do you have the patience to grow into the business over a period of time—say 5 to 8 years?	_______
2. Are you ready and willing to take on additional labor and management responsibilities to operate a farm business in which you have minor ownership?	_______
3. Are you willing to accept and try advice based on the senior generation's experience? Do you have a plan that will continue to involve your senior partner in management of the business?	_______
4. Do you understand that the senior generation has different goals based on retirement needs and that the farm may have to help pay for these needs? Are you willing to help them identify and plan for these needs?	_______
5. Can you accept advice from the senior generation about life, raising a family and family relationships? Are you willing to ask them for help in resolving family and business problems?	_______
Total Points	_______

Answer Key—Total your score from the appropriate tests.*

Total Points Test A	Total Points Test A + B or C	Level of Qualification for farming together
91 – 120	135 – 170	You will make a fine partner
71 – 90	101 – 134	You can make it work
51 – 70	71 – 100	It will be difficult
31 – 50	41 – 70	Don't try it just yet
11 – 30	16 – 40	Little chance of success
0 – 10	0 – 15	No chance!

Note: Sometimes it is more helpful to discuss the areas in which you are the weakest rather than just focusing on the score.

Adapted from *Doing Business Together: A Joint Business Agreement Guide*, NY Farm Link

ADVANCE CARE PLAN

Instructions: Competent adults and emancipated minors may give advance instructions using this form or any form of their own choosing. To be legally binding, the Advance Care Plan must be signed and either witnessed or notarized.

I, ________________________________, hereby give these advance instructions on how I want to be treated by my doctors and other health care providers when I can no longer make those treatment decisions myself.

Agent: I want the following person to make health care decisions for me:

Name: ____________________________ Phone #: ____________ Relation: ____________________
Address: ____

Alternate Agent: If the person named above is unable or unwilling to make health care decisions for me, I appoint as alternate:

Name: ____________________________ Phone #: ____________ Relation: ____________________
Address: ____

Quality of Life:

I want my doctors to help me maintain an acceptable quality of life including adequate pain management. A quality of life that is unacceptable to me means when I have any of the following conditions **(you can check as many of these items as you want)**:

☐ **Permanent Unconscious Condition:** I become totally unaware of people or surroundings with little chance of ever waking up from the coma.

☐ **Permanent Confusion:** I become unable to remember, understand or make decisions. I do not recognize loved ones or cannot have a clear conversation with them.

☐ **Dependent in all Activities of Daily Living:** I am no longer able to talk clearly or move by myself. I depend on others for feeding, bathing, dressing and walking. Rehabilitation or any other restorative treatment will not help.

☐ **End-Stage Illnesses:** I have an illness that has reached its final stages in spite of full treatment. Examples: Widespread cancer that does not respond anymore to treatment; chronic and/or damaged heart and lungs, where oxygen needed most of the time and activities are limited due to the feeling of suffocation.

Treatment:

If my quality of life becomes unacceptable to me and my condition is irreversible (that is, it will not improve), I direct that medically appropriate treatment be provided as follows. **Checking "yes" means I WANT the treatment. Checking "no" means I DO NOT want the treatment.**

☐ ☐ Yes No	**CPR (Cardiopulmonary Resuscitation):** To make the heart beat again and restore breathing after it has stopped. Usually this involves electric shock, chest compressions, and breathing assistance.
☐ ☐ Yes No	**Life Support / Other Artificial Support:** Continuous use of breathing machine, IV fluids, medications, and other equipment that helps the lungs, heart, kidneys and other organs to continue to work.
☐ ☐ Yes No	**Treatment of New Conditions:** Use of surgery, blood transfusions, or antibiotics that will deal with a new condition but will not help the main illness.
☐ ☐ Yes No	**Tube feeding/IV fluids:** Use of tubes to deliver food and water to patient's stomach or use of IV fluids into a vein which would include artificially delivered nutrition and hydration.

PLEASE SIGN ON PAGE 2

Other instructions, such as burial ar

(Attach additional pages if necessary)

Organ donation (optional): Upon my death, I wish to make the following anatomical gift (please mark one):

☐ Any organ/tissue ☐ My entire body ☐ Only the following organs/tissues: ____________

SIGNATURE

Your signature should either be witnessed by two competent adults or notarized. If witnessed, neither witness should be the person you appointed as your agent, and at least one of the witnesses should be someone who is not related to you or entitled to any part of your estate.

Signature: ______________________________ (Patient) DATE: ____________________

Witnesses:

1. I am a competent adult who is not named as the agent. I witnessed the patient's signature on this form. ______________________ Signature of witness number 1

2. I am a competent adult who is not named as the agent. I am not related to the patient by blood, marriage, or adoption and I would not be entitled to any portion of the patient's estate upon his or her death under any existing will or codicil or by operation of law. I witnessed the patient's signature on this form. ______________________ Signature of witness number 2

This document may be notarized instead of witnessed:

STATE OF TENNESSEE
COUNTY OF ____________________

I am a Notary Public in and for the State and County named above. The person who signed this instrument is personally known to me (or proved to me on the basis of satisfactory evidence) to be the person who signed as the "patient". The patient personally appeared before me and signed above or acknowledged the signature above as his or her own. I declare under penalty of perjury that the patient appears to be of sound mind and under no duress, fraud, or undue influence.

My commission expires: ________________ ______________________ Signature of Notary Public

WHAT TO DO WITH THIS ADVANCE DIRECTIVE

- Provide a copy to your physician(s)
- Keep a copy in your personal files where it is accessible to others
- Tell your closest relatives and friends what is in the document
- Provide a copy to the person(s) you named as your health care agent

Approved by Tennessee Department of Health, Board for Licensing Health Care Facilities, February 3, 2005
Acknowledgement to Project GRACE for inspiring the development of this form.

\PPOINTMENT OF HEALTH CARE AGENT

(Tennessee)

I, ______________________________, give my agent named below permission to make health care decisions for me if I cannot make decisions for myself, including any health care decision that I could have made for myself if able. If my agent is unavailable or is unable or unwilling to serve, the alternate named below will take the agent's place.

Agent:	Alternate:
____________________ Name	____________________ Name
____________________ Address	____________________ Address
____________________ City State Zip Code	____________________ City State Zip Code
(____) ____________ Area Code Home Phone Number	(____) ____________ Area Code Home Phone Number
(____) ____________ Area Code Work Phone Number	(____) ____________ Area Code Work Phone Number
(____) ____________ Area Code Mobile Phone Number	(____) ____________ Area Code Mobile Phone Number

____________________ Patient's name (please print or type) Date

____________________ Signature of patient (must be at least 18 or emancipated minor)

To be legally valid, **either** block A **or** block B must be properly completed and signed.

Block A Witnesses (2 witnesses required)

1. I am a competent adult who is not named above. I witnessed the patient's signature on this form.

____________________ Signature of witness number 1

2. I am a competent adult who is not named above. I am not related to the patient by blood, marriage, or adoption and I would not be entitled to any portion of the patient's estate upon his or her death under any existing will or codicil or by operation of law. I witnessed the patient's signature on this form.

____________________ Signature of witness number 2

Block B Notarization

STATE OF TENNESSEE
COUNTY OF ______________

I am a Notary Public in and for the State and County named above. The person who signed this instrument is personally known to me (or proved to me on the basis of satisfactory evidence) to be the person whose name is shown above as the "patient." The patient personally appeared before me and signed above or acknowledged the signature above as his or her own. I declare under penalty of perjury that the patient appears to be of sound mind and under no duress, fraud, or undue influence.

My commission expires: ____________________

____________________ Signature of Notary Public

Approved by Tennessee Department of Health, Board for Licensing Health Care Facilities, February 3, 2005

Sample Attorney Estate Planning Questionnaire

Date:____________________

Full Name:____

Date of Birth:___________ Social Security No.________________ Place of Birth: ________________

Mailing Address: ____

Street or P.O. Box number

____

City State Zip Code

Phone: (Home) ____________________ (Work) __________________ (Cell)____________________

Email Address: ____

Occupation (former if retired) ____

Employer: ____

Spouse: ____

Date of Birth:___________ Social Security No.________________ Place of Birth: ________________

Spouse Occupation (former if retired) ____

Spouse Employer: ____

Date of Marriage: _________ Prior Marriages: Yourself:______________ Spouse: ______________

Names of Children:

A: ____ Date of Birth: ____________________

Name of Child's spouse (if any):____

Mailing Address: ____

Street or P.O. Box number

____

City State Zip Code

Grandchildren: ____

B: ____ Date of Birth: ____________________

Name of Child's spouse (if any):____

Mailing Address: ____

Street or P.O. Box number

____

City State Zip Code

Grandchildren: ____

C: ____ Date of Birth: _______________

Name of Child's spouse (if any):_______________________________________

Mailing Address: ____

Street or P.O. Box number

____

City State Zip Code

Grandchildren: ____

D: ____ Date of Birth: _______________

Name of Child's spouse (if any):_______________________________________

Mailing Address: ____

Street or P.O. Box number

____

City State Zip Code

Grandchildren: ____

List any specific items or amounts that you wish to give to any individuals or organization:

NAME	Item or Amount
______________________________	______________________________
______________________________	______________________________
______________________________	______________________________

Do you have a present will? Yes ________ No ________ (If yes, attach a copy)

Do you have any present living trusts? Yes ________ No ________

If yes, attach a copy and list approximate amount: $ ______________________

Do you anticipate receiving an inheritance? Yes ________ No ________

If yes, give the approximate amount: $ ________________________

Have you given away more than $10,000 to a child or a grandchild, or $3,000 to any other person, in money or property in any single year after 1976? Yes ________ No ________ (If yes, list amounts by years on reverse)

Are you receiving or will you receive an annuity? Yes ________ No ________

If yes, to whom will the payments be made? ____________________________

Is this a life annuity? Yes ________ No ________

Will the amounts continue after your death? Yes ________ No ________

For how long? ____

What will the amount of each payment be? _______________________________________

Do you work for a business which has some type of plan under which your estate or the person you specify will receive benefits on your death? Yes _____ No _____ Not Sure _______

Please attach a copy of your Individual or Employee/Participant Benefit Statement and any information regarding any retirement accounts or pensions.

Who will serve as your Executor? Each spouse for the other: Yes ________ No ________

Someone else? ____

Alternate (if above person(s) unable to serve): ____________________________________

Your choice to act as guardian or your minor children (if applicable):______________________

City and State of residence: ____

Alternate(s):____

City and State of residence: ____

Do you have a safe deposit box? Yes ____ No ____ If yes, where is it located? ______________

Do you own any property if a foreign country? Yes ___ No ___, another state? Yes ___ No ____

Advisors:

Accountant:____

Insurance Agent:____

Investment Advisor:____

Were you referred by anyone? Yes _______ No _______ If yes, by whom? ___________________

LIST OF ASSETS (attach additional sheets if necessary)

	Approximate Values		
	Husband	Wife	Joint
Real Estate: Residence			
Approximate mortgage balance on residence			
Estimated value of furnishings			
Other real estate: (give location, acreage and improvements) Please attach a copy of deeds.			
A.			
B.			
C.			
D.			
E.			

Bank Accounts, Certificates of Deposit, Money Market Funds, etc. Please give name of bank or institution, type of account and approximate balance or value:			
	Husband	Wife	Joint
A.			
B.			
C.			
F.			
G.			
H.			
I.			

Stocks, Bonds, Mutual Funds: Publicly traded stock. Name of corporation and type of shares and exchange on which traded. Please bring copies of most recent statement			
	Husband	Wife	Joint
1.			
2.			
3.			
4.			
Ownership of Business: (corporation, LLC, Limited Ptrn.) Name of business and percentage of ownership: Attach copies of agreements, charter, by-laws or other documentation			
1.			
2.			
3.			

Automobiles, Trucks, Boats	Husband	Wife	Joint
1.			
2.			
3.			
Farm Equipment / Livestock (describe)			
1.			
2.			
3.			
4.			
5.			

Accounts Receivable: Mortgages, Notes or Debts owed to you. Please list debtor's name, date loan made and approximate balance remaining.			
	Husband	Wife	Joint
1.			
2.			

Debts: List any mortgages or other substantial debts owed by you that are not shown above:			
	Husband	Wife	Joint
1.			
2.			
3.			
4.			

Life Insurance:

Company	Face Value	Cash Value	Person Insured	Policy Owner	Beneficiary	Loan Against Policy

Note: Attorney may require signature of both husband and wife if both are using the attorney to prepare wills to insure each understands the attorney is acting as attorney for both and cannot be an advocate for either against the other. All information will be shared by both parties. No confidential information from each party, etc.

WORKSHEET 7.1 Risk Tolerance Quiz

1. In general, how would your best friend describe you as a risk taker?

a. A real gambler
b. Willing to take risks after completing adequate research
c. Cautious
d. A real risk avoider

2. You are on a TV game show and can choose one of the following. Which would you take?

a. $1,000 in cash
b. A 50% chance at winning $5,000
c. A 25% chance at winning $10,000
d. A 5% chance at winning $100,000

3. You have just finished saving for a "once-in-a-lifetime" vacation. Three weeks before you plan to leave, you lose your job. You would:

a. Cancel the vacation
b. Take a much more modest vacation
c. Go as scheduled, reasoning that you need the time to prepare for a job search
d. Extend your vacation, because this might be your last chance to go first-class

4. If you unexpectedly received $20,000 to *invest,* what would you do?

a. Deposit it in a bank account, money market account, or an insured CD
b. Invest it in safe high quality bonds or bond mutual funds
c. Invest it in stocks or stock mutual funds

5. In terms of experience, how comfortable are you investing in stocks or stock mutual funds?

a. Not at all comfortable
b. Somewhat comfortable
c. Very comfortable

6. When you think of the word "risk" which of the following words comes to mind first?

a. Loss
b. Uncertainty
c. Opportunity
d. Thrill

7. Some experts are predicting prices of assets such as gold, jewels, collectibles, and real estate (hard assets) to increase in value; bond prices may fall, however, experts tend to agree that government bonds are relatively safe. Most of your investment assets are now in high interest government bonds. What would you do?

a. Hold the bonds

b. Sell the bonds, put half the proceeds into money market accounts, and the other half into hard assets

c. Sell the bonds and put the total proceeds into hard assets

d. Sell the bonds, put all the money into hard assets, and borrow additional money to buy more

8. Given the best and worst case returns of the four investment choices below, which would you prefer?

a. $200 gain best case; $0 gain/loss worst case

b. $800 gain best case; $200 loss worst case

c. $2,600 gain best case; $800 loss worst case

d. $4,800 gain best case; $2,400 loss worst case

9. In addition to whatever you own, you have been given $1,000. You are now asked to choose between:

a. A sure gain of $500

b. A 50% chance to gain $1,000 and a 50% chance to gain nothing

10. In addition to whatever you own, you have been given $2,000. You are now asked to choose between:

a. A sure loss of $500

b. A 50% chance to lose $1,000 and a 50% chance to lose nothing

11. Suppose a relative left you an inheritance of $100,000, stipulating in the will that you invest ALL the money in ONE of the following choices. Which one would you select?

a. A savings account or money market mutual fund

b. A mutual fund that owns stocks and bonds

c. A portfolio of 15 common stocks

d. Commodities like gold, silver, and oil

12. If you had to invest $20,000, which of the following investment choices would you find most appealing?

a. 60% in low-risk investments 30% in medium-risk investments 10% in high-risk investments

b. 30% in low-risk investments 40% in medium-risk investments 30% in high-risk investments

c. 10% in low-risk investments 40% in medium-risk investments 50% in high-risk investments

13. Your trusted friend and neighbor, an experienced geologist, is putting together a group of investors to fund an exploratory gold mining venture. The venture could pay back 50 to 100 times the investment if successful. If the mine is a bust, the entire investment is worthless. Your friend estimates the chance of success is only 20%. If you had the money, how much would you invest?

a. Nothing

b. One month's salary

c. Three month's salary

d. Six month's salary

Scoring:

1. a = 4; b = 3; c = 2; d = 1
2. a = 1; b = 2; c = 3; d = 4
3. a = 1; b = 2; c = 3; d = 4
4. a = 1; b = 2; c = 3
5. a = 1; b = 2; c = 3
6. a = 1; b = 2; c = 3; d = 4
7. a = 1; b = 2; c = 3; d = 4
8. a = 1; b = 2; c = 3; d = 4
9. a = 1; b = 3
10. a = 1; b = 3
11. a = 1; b = 2; c = 3; d = 4
12. a = 1; b = 2; c = 3
13. a = 1; b = 2; c = 3; d = 4

Key:

0-18	low tolerance for risk
19-22	below average tolerance for risk
23-28	average / moderate tolerance for risk
29-32	above average tolerance for risk
33-47	high tolerance for risk

This quiz is available online at
http://www.rce.rutgers.edu:8080/money/riskquiz/default.asp?

www.farmlandlegacy.org

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