**Passing on the Farm within the Family and Outside the Family**

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The question comes up often about transferring assets to from one owner to the next as retirement plans are developed. Some start planning in their 50’s and early 60’s and some don’t start until they are in their 70’s.

The age that an agriculture producer starts the transfer influences how the process proceeds. In addition, succession plans within the family can look quite different than plans that are developed for outside of the family.

At a minimum, each approach and step should involve both legal and tax professionals to help guide the process along. The addition of a Farm Management Education Program instructor and a lender will also keep the process on track because at some point in time, payments need to be made on time and in line with any agreement.

One question that gets asked often is “How do I transfer the farm if no relative wants to take over?”

In North Dakota, successions within the family have some options available to them that aren’t available to successions that occur outside the family because of the Corporate Farming rules in North Dakota’s Century Code.

An example is Farmer Joe, who is a sole proprietor, wants to be out of production agriculture within five years and has a niece who would like to take over the farm. Due to their kinship, Farmer Joe has the option to set up a Limited Liability Company (LLC) for farm assets and include his niece as a partial owner even if it’s a tiny percentage. Full management control can transfer immediately to the niece and her ownership percentage can grow in three ways. Ownership can be purchased, earned, or gifted. Eventually, ownership of the LLC will be 100 percent with the niece.

If Farmer Joe has no relation that wants to take over, this option is off the table in North Dakota. An example would be a young neighbor that wants to obtain more land, equipment, breeding stock, or facilities. Transferring assets would be done within a sole proprietor to sole proprietor transaction either with contract sale over time or cash sale.

Sole proprietor to sole proprietor transactions is always available to related parties. But the example of a farming LLC is limited by kinship.

Every scenario has its advantages and disadvantages. A common perspective is to look at the income tax consequences and defining a path based on that alone. Although a detailed examination of income tax implications is part of the process, other factors are just as important.

A sole proprietor to sole proprietor sale is very common and can take several different forms like a cash sale or contract sale paid in installments. It is important to realize is that different assets will fall into different asset categories when it comes to taxes and lending. Machinery, for instance, is an intermediate asset that is depreciable for income taxes. Machinery will probably have term payments associated with them regardless of whether the lender is the Farm Service Agency, a private bank, a credit union, or an individual.

A close examination of machinery values and purchase terms are very important. A cash sale is simple. The buyer comes up with the cash. The seller accepts the cash in exchange for the piece of equipment. The buyer now has a value or “basis” that can be depreciated over time on the buyer’s income tax forms, but the seller must claim the cash sale purchase price minus the undepreciated value “remaining basis”. In many cases the seller has no remaining depreciation value left and must claim 100% of the sale price as re-captured depreciation. This is ordinary income just like a grain or calf sale.

Machinery sales under contract over several years are handled very similar in the fact that the entire sale price must be claimed in that first year of the contract. Thus, having the same re-captured depreciation as a cash sale even though not all payment is received in that year.

Machinery rental is handled quite differently. If machinery and land are under the same rental contract, the money comes in as rental income rather than ordinary income. The two types of income are handled differently on Joe Farmer’s income tax return.

Transferring land and raised breeding livestock are handled differently from machinery. Land is considered a capital asset. Gains, or losses in some cases, are calculated as the sale price minus the purchase price or inherited value. A positive number is taxed at capital gains rates rather than the ordinary income rates. A positive capital gain in land sales paid overtime are taxed based on the amount of principal paid within a particular year under the contracted scheduled payment.

Breeding livestock raised by Joe Farmer is similar but not identical. Costs for raising these animals have already been expensed in previous years. Principal payments on a contract of scheduled payments will be taxed as a capital gain. Purchased breeding stock like bulls will be taxed as re-captured depreciation, similarly to machinery.

Many options and opportunities exist when making these succession decisions. North Dakota Farm Management Education Program instructors across the state can aid in making the decisions that are right for these situations that are structured for individual circumstances.

To learn more about farm succession planning and other financial questions about farms and ranches, visit with an instructor near you. The North Dakota Farm Management Education Program provides lifelong learning opportunities in economic and financial management for persons involved in the farming and ranching business. Visit [ndfarmmanagement.com](http://www.ndfarmmanagement.com), Facebook @NDFarmManagementEducation, or contact Craig Kleven, State Supervisor for Agricultural Education, at crkleven@nd.gov or 701-328-3162 for more information. The ND Farm Management Education Program is sponsored by the North Dakota Department of Career and Technical Education.

**Disclaimer:** Kyle Olson is not a tax or legal professional. He is a Farm Management Education Program instructor. Please consult Tax and Legal professionals for specific rules, methods, and filings.