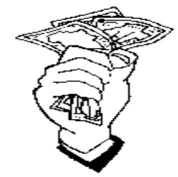
Keeping the Estate Tax



Sean McCann

Many is the year that a good calving season is decimated by disease, weather or coyotes. It's a simple thing to call the vet, and with a lot of hard work a snowbound herd can be nourished through a storm. Unfortunately recent legislation has made it increasingly difficult to get the coyotes. Similarly, modern ranchers are more susceptible than ever to estate losses due to "tax coyotes" that can eat up 55% of an estate's value. While other high net worth individuals have much of their estate in financial assets, agricultural wealth usually is tied up in acreage, equipment, livestock and other commodities. This leaves the agricultural estates of most ranchers cash poor upon their death, and the IRS does not operate on the barter system.

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Today, an estate worth $2,000,000 is required to pay a tax of $780,800 due within nine months of death (this tax rises astronomically with larger estates). Typically an estate of this size will have a tax credit of $202,050 (1998 figure), providing the deceased did not make excessive lifetime gifts. After applying this credit, the tax bill is still in excess of $575,000! Coming up with enough cash to pay this bill is a tough order for any producer, let alone a temporary manager called on to work only during an estate's settlement period.

The executor(s) or personal representative(s) of the estate must first drain what cash is available and then are forced to sell off assets to pay the bill. Stored grain and livestock go first as they are the most liquid, and the market dictates the price. If you died when these commodities were at a premium, your estate might benefit, but there is not a lot of leeway if the price is low. Even after selling these liquid assets most of the tax bill is often left unpaid. Equipment comes next, and that great deal you got on old so-and-so's grinder becomes an even better deal for the guy whose cows have been doing the two-step with your bull without paying for the dance!

The executor(s) may try to retain some equipment so that your heirs can continue to produce, but usually that means turning to the most durable of all farm goods, LAND!! This will command better prices than equipment, and often will sell for more than what you thought it was worth, with land more and more difficult to obtain.

Before you can say "hailstorm coming" the $2,000,000 farming operation you spent your lifetime putting together is cut in half (and other creditors and estate settlement advisors have yet to be paid). Part of the ranch that's been in your family for years is now under new ownership, and what is left to your family may be difficult to manage, given the lack of equipment and capital. This is the last thing most men and women of the land want as their legacy.

How can this be prevented? The answer lies in *estate conservation planning*. This is the science of preventing estate erosion, and involves the right mixture of simple and complex techniques. The process can be simplified by developing the right estate planning team. Begin by finding an expert who specializes in estate conservation. Make sure their reputation extends beyond your hometown. This might be an accredited life insurance agent (CLU, ChFC, or CFP), a tax attorney (LLM) or a CPA with an estate planning focus. If the normal person who handles your insurance, legal or tax work does not specialize in this area, then be prepared to extend your search.

One place to find the expert is through successful producers who recently updated their estate plans. Estate planning is a complex, ever changing process, and many people with perfect plans five years ago now have one that's full of holes. Last year (1997) was a key year for changes, most of which greatly benefited the agricultural producer, and therefore all pre-1997 plans need review. Ask for and check the references of anyone you don't know, and be wary of anyone who can solve your problems quickly without getting to know you, your operation and your dreams for the future.

The ideal estate planning expert will be a cross between a coach and a quarterback as they guide you through the process. They should be able to prove their knowledge and competence to you with a thorough analysis of your situation that you can understand. They should be adept in the use of various techniques based on the different scenarios for your future (you die first, your spouse dies first, you die together, etc.). Any plan they design should be a natural fit, and not a pre-packaged gimmick that "works" for everyone.

At some point your estate planner should suggest the involvement of specialists from other fields. These individuals should not complicate the process. Attorneys are needed to draft legal documents such as wills and trusts, life insurance agents and financial planners can provide funding for estate taxes, and accountants and tax attorneys can give advanced tax advice. They all should be able to work seamlessly with your life-long advisors.

Everyone needs some estate planning, and if you have assets in excess of $625,000 and do not want to see the government as one of your primary beneficiaries, then it is especially important you uncover some of the facts pronto! Two weeks spent working on your estate will be more valuable to your survivors than ten years of expanding herds. It is particularly important to plan now if your spouse is living in order to capitalize on a second estate tax credit of $202,050. A qualifying farm/ranch exemption might save an additional $200–300K in taxes on each spouse's estate. It is important to note each properly applied credit lowers your tax bracket, and saves more money from taxation. Finally, it is possible to put off all taxes until death of both spouses, which can significantly reduce or altogether eliminate the bill.

Estate planning becomes more expensive as you get older, and your options will decrease, so it's best to bite the bullet early. Life insurance, wills, trusts, gifting and asset shifting can all be involved and the use of these techniques gets more complicated with age. The proper applications of these tools are the estate planner's best weapon against a pack of howling IRS coyotes. With education, most ranchers realize the importance of these methods, and embrace their usage, so its important to seek out the right solutions with an open mind. It might help to keep in mind that there are not too many lawyers and insurance agents who appreciate the essence of a summer feed lot, but that has not stopped them from eating T-bone!

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