



Legal Considerations for the Farm Transition Process

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Transition Planning Tax Considerations

Federal and State Taxes

- Federal Estate and Gift Taxes
- Pennsylvania Inheritance Tax
- Income Taxes
- Capital Gains
- FICA and Self-Employment
- Realty Transfer Tax
- Capital Stock (repealed 1/1/2016)
- Real Estate Taxes / Clean and Green Issues



Transition Planning Tax Considerations

Federal Estate and Gift Taxes

- The federal estate and gift tax applicable exclusion amount for 2025 is \$13.99 million (to permanently increase to \$15 million in 2026 as a result of the One Big Beautiful Bill Act) plus the deceased spouse's unused, preserved exclusion (DSUE).
- The federal annual gift exclusion amount is \$19,000 for 2025 and is tied to inflation with changes in \$1,000 increments. The amount will remain at \$19,000 for 2026.
- The federal estate and gift taxes impact VERY few taxpayers with approximately \$14M applicable exclusion amount (\$28M per couple and for a surviving spouse, if preserved by filing a 706 at spouse's death).



Transition Planning Tax Considerations

Pennsylvania Inheritance Tax

- Rates
 - spouse – 0%
 - direct beneficiaries – 4.5%
 - siblings – 12%
 - others – 15%
- Ag Exemptions (effect. 7/1/2012)
 - Farmland – Other Exemption
 - Business of Agriculture Exemption
- Family Business Exemption (effect. 7/1/2013)



Transition Planning Tax Considerations

Pennsylvania Inheritance Tax



- Farmland - Other Exemption
 - §9111(s.1) - Transfers to or for the benefit of lineal descendants or siblings of an agricultural commodity, agricultural conservation easement, agricultural reserve, agricultural use property, and forest reserve are exempt from inheritance tax.
 - Agricultural commodity is defined as “any and all plant and animal products, including Christmas trees produced in Pennsylvania for commercial purposes.”
 - No 7-year look-back.

Transition Planning Tax Considerations Pennsylvania Inheritance Tax

- Business of Agriculture Exemption
 - §9111(s) - Real estate devoted to the “business of agriculture” is exempt from inheritance tax if it:
 - (1) is transferred to or for the benefit of members of the same family;
 - Extends to second cousins
 - (2) is devoted to the business of agriculture at the time of decedent’s death and must continue for a period of seven (7) years after the owner’s date of death; and
 - (3) produces annual gross income of at least \$2,000 in the business of agriculture for a period of seven (7) years after the decedent’s date of death.
 - Annual certification required to Department of Revenue.





Transition Planning Tax Considerations Pennsylvania Inheritance Tax

- Family Business Exemption
 - §9111(t) - A transfer of a qualified family-owned business interest to or for the benefit of members of the same family is exempt from inheritance tax if it:
 - continues to be owned by members of the same family or a trust whose beneficiaries are comprised solely of members of the same family for a minimum of seven (7) years post-death; and
 - is reported on a timely filed inheritance tax return.
 - The exemption does not apply to property transferred into the qualified family-owned business within one year of the decedent's death, unless transferred for a "legitimate business purpose."
 - Annual certification requirement (7 years).

Transition Planning Tax Considerations **Stepped-up Basis**

- Tax basis of assets acquired from decedent is adjusted at death to fair market value.
- Tax basis of assets transferred during lifetime by gift is carried over.





Transition Planning Tax Considerations

Summary of Liquidity Needs at Death

(\$3,500,000 Estate)

1. Funeral.....	\$20,000
2. Miscellaneous.....	\$10,000
3. Attorney	\$70,000
4. Executor	\$70,000
5. PA Inheritance Tax	\$22,500*
6. Federal Estate Tax	\$ 0
CASH NEEDED.....	\$192,500

*Takes into account the ag/family business exemptions, which save \$135,000 of tax.

Transition Planning Tax Considerations Cash Needs of Farm Child

Farm/Business Assets

\$3,000,000

Liquid Assets

\$500,000

3 Children

1 Farm/Business Child

Assume Equal Division

Farm/Business Child Needs

\$1,897,500



Transition Planning Tax Considerations

Succession Planning Techniques

(2025 Example)

- Fair Market Value\$1,800,000
 - Sale Price \$600,000
 - Gift\$1,200,000
 - F & M to S & D-in-L (annual exclusions).....\$76,000
 - Gift Credits Used\$1,124,000
 - \$562,000 of Father's with \$13,428,000 remaining
 - \$562,000 of Mother's with \$13,428,000 remaining
-
- Death Credits Remaining.....\$26,856,000
(under most circumstances)



Transition Planning Legal Considerations

Lifetime Transfers



"Sign here to indicate you have no idea what you've signed for."

- Legal Tools
 - Deed of Gift
 - Lease
 - Sale with lump-sum or installment payments
 - Sale through self-cancelling installment obligation
 - First right to purchase and option agreements
 - Transfer of ag conservation easements
 - Life insurance
 - Legal entity for joint ownership
 - Buy/Sell agreements

Transition Planning Business Considerations **Entity Planning**

- Limited liability company (LLC)
 - Quickly becoming most popular option
 - Conversion available (7/1/2015)
- Sole Proprietorship
- Corporation
- Partnership
- Trust





Transition Planning Business Considerations

Entity Planning

- Limited Liability Company
 - Owner is referred to as member
 - Can be member-managed or manager-managed
 - Available for sole owner/operator
 - Limited liability for each member
 - Either 1040 for single member or 1065 for >1 member, but can elect to be taxed as a corporation and use Form 1120
 - Presently the entity of choice in farm operations, especially if >1 owner/operator

Transition Planning Business Considerations **Entity Planning**

- Limited Liability Company (cont'd.)
 - No longer subject to capital stock tax (repealed)
 - Realty transfer tax family farm exemption if qualify
 - Operating agreement/buy-sell provisions recommended
 - Self-employment/Social Security tax planning for a corporation also available to LLC if taxed as a corporation





Transition Planning Business Considerations **Entity Planning**

- Sole Proprietorship
 - Most simple/common farm business form
 - For sole owner/operator
 - No liability protection
 - Form 1040 tax return
 - Possibly multiple sole proprietorships if >1 owner/operator, but co-ownership agreement with buy-sell provisions recommended
 - Familial exemptions for realty transfer tax



Transition Planning Business Considerations **Entity Planning**

- Corporation
 - Owner is referred to as shareholder
 - C cf. S corporation – tax, not legal difference
 - Available for sole owner/operator
 - Limited liability for each shareholder
 - Form 1120 for C and Form 1120S for S corporations
 - Less common with farm operations due to potentially severe tax consequences upon dissolution, but some Social Security/FICA advantages possible for high income businesses



Transition Planning Business Considerations **Entity Planning**

- Corporation (cont'd.)
 - No longer subject to capital stock tax (repealed)
 - Realty transfer tax family farm exemption if qualify
 - Buy-sell agreement recommended



Transition Planning Business Considerations **Entity Planning**

- General Partnership
 - Owner is referred to as partner
 - When >1 owner/operator
 - All partners are general partners
 - No limited liability protection
 - Form 1065 for tax return
 - Common farm business form when >1 owner/operator, but giving way to LLCs
 - Partnership agreement with buy-sell provisions recommended
 - Realty transfer tax family farm exemption if qualify

Transition Planning Business Considerations

Entity Planning

- Limited Partnership
 - Unlike general partnership, also has limited partner(s)
 - Owner owns either limited partner or general partner interests
 - Limited liability for limited partner(s), not for general partner(s) (unless LLC or corp. as general partner)
 - Form 1065 for tax returns
 - Historically used for real estate ownership for non-active owners, such as extended family members, but this has changed now that capital stock tax is repealed
 - Partnership agreement with buy-sell provisions recommended
 - Realty transfer tax family farm exemption if qualify



Transition Planning Business Considerations Entity Planning

- Trust
 - Trustee is usually non-owner (the “manager”)
 - Beneficiary is person(s) entitled to receive the financial benefits of the trust
 - There are many types and purposes of trusts, such as revocable trust, irrevocable trust, asset protection trust, dynasty trust, testamentary trust, grantor trust, supplemental needs trust, etc.
 - Not common for farm business operations, but slightly gaining in popularity for real estate ownership
 - Form 1041 for tax returns
 - Prudent investor/fiduciary issues
 - Principal and Income Act issues





Transition Planning Legal Considerations Transfers at Death – Estate Planning

- Wills
 - Key Safety Net for Transition Plan
 - Distribution Arrangements
 - Fiduciaries –
Executor/Trustee/Guardian
 - Tax-Saving/Disclaimer Will

Transition Planning Legal Considerations

Estate Planning



- Powers of Attorney
 - New Requirements in PA - effective January 1, 2015 and January 19, 2021
 - Financial and Health Care combined?
 - Sole/Multiple/Joint Agents?
- Health Care Declarations (Living Wills)
 - Organ donation?
 - Instructions for Agent(s)

Transition Planning Legal Considerations **Estate Planning**

- Non-Tax Considerations
 - Marital Issues
(i.e., divorce)
 - Pre/Postnuptial
Agreements
 - Probate/Non-Probate
 - Oil & Gas/Solar Interests
 - Digital Assets
 - Elder Law Issues



Transition Planning Legal Considerations Elder Law Planning

- Daily gift penalty divisor = \$399.80/day (2025)
- Resource allowance - \$2,400 (to \$8,000 for lower income)
- Minimum \$31,584 - Maximum \$157,920 - Community Spouse Resource Allowance (2025)
- Personal Residence Equity – generally up to \$730,000 (2025)
- Installment Notes – must be Medicaid compliant or revised
- Long Term Care Insurance





Transition Planning Legal Considerations

Elder Law Planning

- Latest Planning Techniques:
 - Possible Annuity Purchase to Accelerate Qualification
 - Grantor Trusts
 - Family Caregiver Agreements – agreement must be in writing
 - Transfer of Assets to Community Spouse
 - Re-Write Community Spouse's Will



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