More Legal and Tax Issues Involving Farmers and Ranchers

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Overview

With today's article I look at more legal and tax issues that farmers and ranchers need to know about. Being aware of legal and tax issues is a means of overall risk management for the operation.

More discussion of legal and tax issues – it's the topic of today's post.

Getting Sued in Another State – The Personal Jurisdiction Issue

Walters v. Lima Elevator Co., 84 N.E.3d 1218 (Ind. Ct. App. 2017)

If you engage in a business transaction involving your farm or ranch in another state and a lawsuit is filed based on that transaction, does that state's legal system have jurisdiction over you? In 1945, the U.S. Supreme Court said that a party (particularly a corporation or a business) could be sued in a state if the party had "minimum contacts" with that state. *International Shoe Company v. State of Washington, 326 U.S. 310 (1945).* Over time, many courts have wrestled with the meaning of "minimum contacts," but it basically comes down to whether the party is deriving the benefit of doing business with that particular state or is sufficiently using the resources of that state. That's oversimplifying the application of the Court's reasoning, but I think you get the point.

In terms of applying the "minimum contacts" theory to farm businesses, a recent case provides a good illustration. In the case, a Michigan farmer ordered seed from an Indiana elevator about 20 miles away. It was the third time he had done this. He bought the seed on credit, and when it was ready he went to the elevator to pick it up. When he didn't pay for the seed, the elevator sued him in the local court in Indiana. He sought to dismiss the case on the basis that the Indiana court didn't have jurisdiction over him. He claimed that he lacked sufficient minimum contacts with Indiana to be sued there. The court disagreed. The Michigan farmer had "purposely availed" himself of the privilege of conducting business in Indiana. Because of that, the court reasoned, he could have reasonably anticipated being subject to the Indiana judicial system if he didn't pay his bill. His due process rights were also not violated – his farm was less than 20 miles away from the Indiana elevator.

If you intentionally conduct business in a state and are sued as a result of your contacts and actions with that state, that state's courts will likely have personal jurisdiction over you.

Social Security Planning for Farmers

Introduction

Part of retirement planning for a farmer includes Social Security benefits. Relatedly, if you are nearing retirement age you might be asking yourself when you should start drawing Social Security benefits. The answer is, “it depends.” But there are a few principles to keep in mind.

The first point to keep in mind is that maximum Social Security benefits can be received if you don’t withdraw benefits until you reach full retirement age – that’s presently between ages 66 and 67. Additional benefits can be achieved for each year of postponement until you reach age 70. Another point is that some Social Security benefits are reduced once certain income thresholds are reached. For 2024, if you haven’t reached full retirement age and earn more than $22,320, benefits get reduced $1 for every $2 above the limit. During the year in which you reach full retirement age, the earnings limit is $59,520 with a $1 dollar reduction for every $3 dollars over the limit. Once you hit full retirement age, the limit on earning drops off.

In-kind wages count toward the earnings limitation test, but employer-provided health insurance benefits don’t. Also, federal farm program payments are not earnings for years other than the first year you apply for Social Security benefits.

So, when should you start drawing benefits? It depends on your particular situation and your retirement plan. The Social Security Administration has some useful online calculators that can help. Check out ssa.gov.

Common Estate Planning Mistakes of Farmers

What are some common mistakes that farmers and ranchers make when it comes to estate planning?

Consider the following:

- Not ensuring title ownership of property complies with your overall estate planning goals and objectives. This includes the proper use of jointly held property, as well as IRAs and other documents that have beneficiary designations.
- Not knowing what the language in a deed means for purposes of passage of the property at death.
- Leaving everything outright to a surviving spouse when the family wealth is potentially subject to federal estate tax.
- Thinking that “fair” means “equal.” If you have both “on-farm” and “off-farm” heirs, the control of the family business should pass to the “on-farm” heirs, and the “off-farms” heirs should get an income interest that is roughly balanced in value to that of the “on-farm” heirs’ control interest. Leaving the farm to all the kids equally is rarely a good idea in that situation.
- Letting tax issues drive the process.
- Not preserving records and key documents in a secure place where the people that will need to find them know where they are.
- And not routinely reviewing your plan. Life events may have changed your goals or objectives.

I could list more, but these are some big ones. Try to avoid these mistakes with your estate plan.

When is a Partnership Formed?

Farmers and ranchers often do business informally. That informality can raise a question of whether the business arrangement has created a partnership. If that is determined to be the case, numerous legal issues might be created.

A big potential issue is that of unlimited liability. Partners are jointly and severally liable for the debts of the partnership that arise out of partnership business. Also, a partnership files its taxes differently than do individuals, and assets that are deemed to be partnership assets could pass differently upon the death of someone deemed to be a partner.

So how do you know if your informal arrangement is a partnership? From a tax standpoint, if you're splitting net income from the activity rather than gross, IRS could claim the activity is a partnership. While simply jointly owning assets is not enough, by itself, to constitute a partnership, if you refer to you and your co-worker as "partners" or create a partnership bank account or fill out FSA documents as a "partnership," a court could conclude the activity is a partnership. Most crop-share or livestock share leases are not partnerships, but you must be careful. It's best to execute a written lease and clearly state that no partnership is intended if you don't want questions to come up.

The IRS missed asserting that an informal partnership arrangement had been created by a mother and her daughter in a Tax Court case last year involving an Oklahoma ranch, and also lost on a hobby loss argument. *Carson v. Comr., 2024 U.S. Tax Ct. LEXIS 1624 (U.S. Tax Ct. May 18, 2023).* Don't count on IRS missing the same arguments in your situation.

Conclusion

There will be more issues to discuss next time.