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Does the Federal Estate Tax Impact Farm Transition?

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Market Report	Yr Ago	4 Wks Ago	9/29/06
Livestock and Products, Weekly Average			
Nebraska Slaughter Steers, 35-65% Choice, Live Weight	$86.44	$90.96	$90.83
Nebraska Feeder Steers, Med. & Large Frame, 550-600 lb	136.86	132.92	128.57
Nebraska Feeder Steers, Med. & Large Frame 750-800 lb	120.88	122.32	117.10
Choice Boxed Beef, 600-750 lb. Carcass	137.56	145.57	141.34
Western Corn Belt Base Hog Price Carcass, Negotiated	68.05	66.42	61.25
Feeder Pigs, National Direct 45 lbs, FOB	52.36	53.56	52.76
Pork Carcass Cutout, 185 lb. Carcass, 51-52% Lean	70.37	76.14	67.17
Slaughter Lambs, Ch. & Pr., 90-160 lbs., Shorn, Midwest	94.37	94.25	99.62
National Carcass Lamb Cutout, FOB	243.84	232.05	245.47
Crops, Daily Spot Prices			
Wheat, No. 1, H.W. Imperial, bu	*	4.35	4.46
Corn, No. 2, Yellow Omaha, bu	1.52	2.06	2.38
Soybeans, No. 1, Yellow Omaha, bu	5.19	4.91	4.92
Grain Sorghum, No. 2, Yellow Columbus, cwt	2.45	3.38	3.68
Oats, No. 2, Heavy Minneapolis, MN , bu	1.80	2.12	2.25
Hay			
Alfalfa, Large Square Bales, Good to Premium, RFV 160-185 Northeast Nebraska, ton	117.50	135.00	135.00
Alfalfa, Large Rounds, Good Platte Valley, ton	37.50	87.50	87.50
Grass Hay, Large Rounds, Good Northeast Nebraska, ton	52.50	82.50	82.50

* No market.

Statistics show that the Federal Estate Tax impacts an extremely small number of farms and ranches. A Congressional Budget Office report based on data from the year 2000 projects less than 125 estates that own agricultural property would pay Federal Estate Tax nation wide.

It might be useful to examine what triggers the need for an estate to pay Federal Estate Tax. Under current law, when someone dies, the estate of the decedent must file a Federal Estate Tax return if the net value of the estate is greater than the Federal Estate Tax exclusion amount. Taxes must be paid on the net estate value over the exclusion amount (minus some deductions). The exclusion amount for 2006–2008 is $2,000,000 per person. If a husband and wife own property together and do some appropriate planning, the two of them can each take advantage of their exclusion and effectively double the Federal Estate Tax exclusion amount, therefore in 2006 – 2008 a couple could pass on an estate valued at $4,000,000 to their heirs and have $0 Federal Estate Tax due. The exclusion amount increases from $2,000,000 to $3,500,000 in 2009. In 2010 the Federal Estate Tax exclusion is unlimited, therefore no one will pay Federal Estate Tax in 2010 if the law is not changed. In 2011 however, the Economic Growth and Tax Relief Reconciliation Act of 2001 is scheduled to expire and the Federal Estate Tax exclusion amount will revert back to $1,000,000 per person.

There has been much debate regarding the impact of Federal Estate Tax on farmers and ranchers. It has been suggested that paying Federal Estate Tax or "Death Tax" as it has been called, jeopardizes succession of family farms and small businesses to the next generation. Let's look at some historical facts. Roger McEowen, Associate Professor of Law at Iowa State University has compiled the following statistics:

Table 1.

	2001	2003
Exclusion Amount	$675,000	$1,000,000
Decedents/Year	2,300,000	2,300,000
Taxable Estates/Year	51,841	30,627
Taxable Estates with Agricultural Property	2,602	1,966

In 2001, with an exclusion amount of $675,000; 51,841 or 2.3 percent of the decedents had estates large enough to trigger a Federal Estate Tax obligation. The 51,841 taxable estates included 2,602 estates that owned agricultural property. In 2003, the exclusion amount had risen to $1,000,000 resulting in 30,627 or 1.3 percent of decedents with taxable estates. The 30,627 taxable estates included only 1,966 that owned agricultural property. Table 1 demonstrates how a rise in the exclusion amount lowers the number of taxable estates as well as the taxable estates with agricultural property.

Table 2 shows taxable estates with agricultural property numbered at 2,602 (.11 percent of all decedents) in 2001. The vast majority (2,108 or 81 percent) of the estates with agricultural property were under $2,500,000. In 2003 the exclusion amount was raised to $1,000,000 and the taxable estates with agricultural property dropped to 1,966 (.09 percent of all decedents) with (1,309 or 67 percent) under $2,500,000. Less than one tenth of one percent of all decedents had taxable estates that included agricultural property in 2003. The exclusion amount has since doubled to $2,000,000 (2006–2008) and is scheduled to rise to $3,500,000 in 2009.

Table 2.

Taxable Estates with Farm Property/Year	2001	2003
Estate Size:		
$625,000-$1,000,000	916	NA
$1,000,000-$2,500,000	1,192	1,309
$2,500,000-$5,000,000	319	392
$5,000,000-$10,000,000	71	139
$10,000,000-$20,000,000	60	65
Over $20,000,000	44	61
Total	2,602	1,966

The Congressional Budget Office report dated July 2005 entitled "Effects of the Federal Estate Tax on Farms and Small Businesses" examined data from the year 2000 and extrapolated the impact of raising the Federal Estate Tax exclusion amount to project the number of estates that would have owed Federal Estate Tax if higher exclusion amounts were applied to the 2000 data. In the year 2000 the exclusion amount was $675,000. There were roughly 52,000 taxable estates that year with 1,659 of those estates owning agricultural property. If the exclusion amount were raised to $1,500,000 it would have lowered the taxable estates to 13,771 with 300 estates owning agricultural property. By raising the exclusion amount to the 2006–2008 level of $2,000,000, taxable estates dropped to 6,337. Those with agricultural property were projected at 123. If raised to the 2009 exclusion amount of $3,500,000 taxable estates were projected to be 3,676. Those that included agricultural property were only 65.

Does Federal Estate Tax impact farm transition? The statistics indicate the answer is no. There are very few farms or ranches that can't minimize or completely eliminate Federal Estate Tax obligations if proper planning is implemented. Inflation has increased the value of farm assets, especially land, but the $3,500,000 exclusion level set for 2009 would allow all farm families to pass $7,000,000 to the next generation with $0 in Federal Estate Tax. A relatively high exclusion such as $3,500,000 would still generate a substantial amount of tax revenue but have only a minor impact on agricultural estates.

There is another factor in the Federal Estate Tax debate that has been overlooked by many, the loss of a "stepped up basis." Elimination of the step up in basis could be very costly to many farm families. Current law provides for an increase in the basis for agricultural property when passed to the next generation through a time of death transfer. Some proposed legislation would reduce or eliminate the step up in basis, resulting in a Capital Gain Tax obligation being generated if an heir were to sell inherited agricultural property. This could potentially create a much more relevant impact on heirs of average family sized farms and ranches and would have a much larger impact on agriculture in general if loss of the step up in basis were to become law.

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