



# Farmers First Trust

## Preserving Value



## Fixing the Balance Sheet

# While Preserving the Value of Your Farm

Gaining financial strength through difficult times.

[farmersfirsttrust.com](http://farmersfirsttrust.com)

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## Introduction

This white paper will not dwell on the financial stress faced by today's farmer because every farmer is feeling the pinch in cash flow especially when talking with their banker. Our focus will be on an approach to improve the balance sheet and continue farming.

Our guidelines for this whitepaper will be:

- 1) Improving the balance sheet and
- 2) Continue to farm

For the banker, improving a farmer client's balance sheet provides the flexibility to work with the farmer without 'guidance' from the loan committee.

For the farmer, a better balance sheet provides a stronger baseline to make changes to the farm operation to respond to new revenue opportunities and overcome challenges.

## Scenario

The foundational element needed for this approach is farm (ranch) land ownership. Farmers can sell machinery, buy used or rent critical but sparsely used pieces of machinery to improve cash flow and help the balance sheet. But our focus is farm (ranch) land ownership.

**Farm Location:** Any state in the United States.

**Farm Operation Scenario:** The fourth generation is beginning their involvement with the farm operation, even though they are still in high school. Each generation has added owned and rented farmland that has grown the operation to more than 6,000 acres.

**Owned acres:** 850 acres

**Rented acres:** 5,700 acres (cash rent)

**Row crop:** Corn and soybean rotation

**Livestock:** None, cow/calf operation sold over 10 years ago

**New crop ideas:** Investigating organic corn and soybeans for higher profitability.

**Issue:** Investment in equipment to support organic requirements will cost time and money.



## Decision Criteria

In our scenario, the decision was made to sell 320 contiguous acres under contract that provide the following lease buyback terms:

- Annual cash rent – a percentage of purchase price
- Buyback Option Increase of ‘agreed to’ % annually of purchase price, with five- or ten-year call.

*Note:* Most farmer do NOT want to sell any of their owned land. Terms will/should be negotiated that provides a way back for the farmer to own the land. The terms in this land sale are such that once the balance sheet is healthy and the plan for a new commodity direction has firm footing, the farmer has a contractual option to buy back the land.

**Sale price/acre:** \$5,700/acre

**Acres Sold:** 320

**Total sale \$’s:** \$1,824,000

**Basis per acre:** \$885/acre

**Basis:** \$283,200

**Exposure to capital gains taxes:** \$492,582

Tax Type	Marginal Tax Rate	Effective Tax Rate	Tax Amount
Federal	23.80%	22.26%	\$342,997
State	8.98%	8.98%	\$138,364
Local	0.73%	0.73%	\$11,221
Total Capital Gains Taxes			\$492,582

*NW Iowa location used for taxes shown.*

*Numbers shown are for example only and does not represent your tax situation.*

**Closing costs (est.):** \$100K

The farm operation will be paying almost \$500K in capital gains taxes, leaving \$1.2M to pay off debt and improve the balance sheet. The bank is in a better situation with the \$1.2M paid against the liabilities, but what if the farmer could defer the \$500K? How could that be made possible?



## Deferring the Capital Gains Tax

First thing to remember, the capital gains tax can be deferred for up to 30 years, but it will be due at the term end, in 30 years!

What are the steps the farm operation can review to determine if they should defer their capital gains taxes? Let's take a look:

Activity	Standard Tax Approach	MDPT - Deferring Capital Gains Taxes
Net Sale (after closing costs)	\$ 1,724,000	\$ 1,672,324
Capital Gains Tax Paid (current year)	\$ 492,582	\$ -
Cash available after transaction	\$ 1,231,418	\$ 1,588,708
Additional cash available with MDPT		\$ 357,290

See <https://www.farmersfirsttrust.com> for details of calculation methodology.

The MDPT process provides up to 95% of the net sale as cash (in the form of a low-cost loan) for the farm operation to invest in the farm, pay off additional debt or other as they desire.

Here is the catch...the farm operation will be paying approx. 1.2 – 1.5% interest only on the \$1,588,708 each year. Is it really a catch? Farmers are typically comfortable with paying anywhere from 4.5% to 9% for a Line of Credit (LOC) each year to put a crop in the ground. Now, think of it as a LOC for only 1.2% or so.

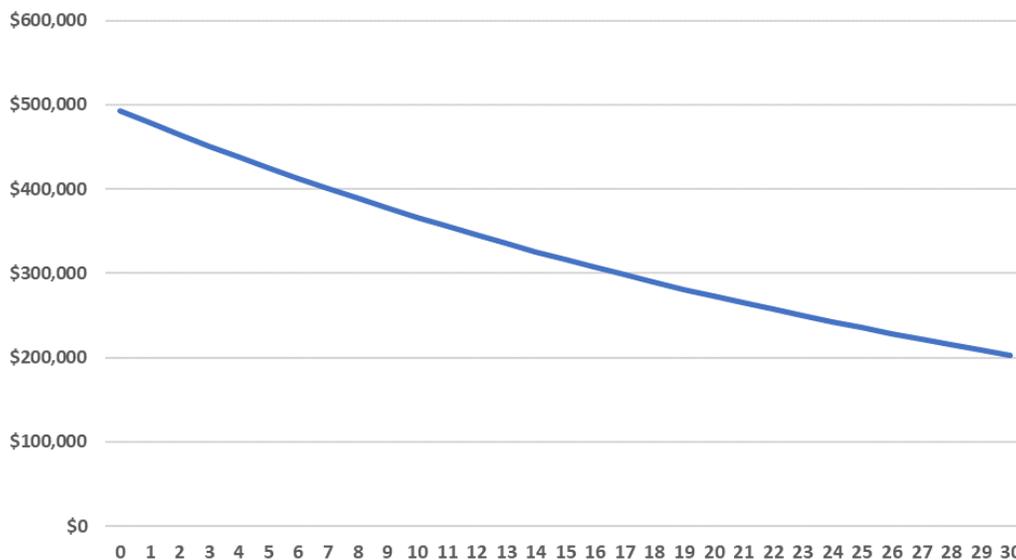
Monetized Deferred Payment Transaction MDPT, utilizes Section 453 of the US tax code and is therefore not encumbered by the restrictions placed on 1031-Exchange transactions.



## The Power of Present Value

Present value accounts for the time value of money. Over time, even 3% inflation erodes the power of the dollar so paying in the future is paying with cheaper dollars. Delaying payment of taxes allows you to pay with comparably inexpensive dollars in the future!

When the deferral timeframe has arrived, the capital gains taxes will be due. However, compared to today's dollars, they will be significantly reduced. If we calculate a 3% inflation rate (realistically it will go up and down over 30 years and what that fluctuation will be is anyone's guess.) on \$492,582 we see how the power of present value works in the favor of the farm operation:



Because of time and inflation, \$492,582 is reduced (comparable to today's \$'s) to a little over \$200K which is about 59% less than if the taxes were paid in the standard fashion!

The key is to grow the deferred dollars, allow inflation and time to work on the real dollar payment due in 30 years and get your farm operation cash flowing positively.

Financial institutions establish their strategic plans and future investments based upon present value. MDPT allows farmers to leverage the power of present value for the benefit of their farm operations.



## Conclusion

The Monetized Deferred Payment Transaction MDPT is a powerful approach for farm operations seeking ways to preserve the value of their farm. Receiving cash (in the form of a loan) will provide a financial improvement that can be utilized in a way that is most beneficial to the farm.

If your farm financials have been pressed down due to commodity prices and you are able to sell farmland to boost the balance sheet, by all means take a look at MDPT and preserve the funds from the sale.

Monetized Deferred Payment Transaction MDPT, see [farmersfirsttrust.com](http://farmersfirsttrust.com) for details and background information.

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