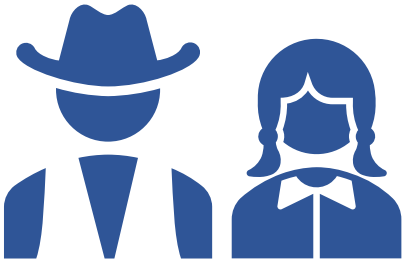
Farmers First Trust
Preserving Value



I'm Cashing In

I Have Loved Farming – Now it is Time to Sell it All

A Farm Couple's Decision to Preserve the Value and Heritage of their Farm.

farmersfirsttrust.com

Introduction

Have you ever thought of selling the farm and retiring? Most farmers that have been farming for four or five decades have answered 'yes' to that question, if only in their thoughts. But their love of the land and everything accomplished in their operation over those decades keeps them from following through. Some farmers go the next step to think through what is required to sell it all.

While it may sound and feel good to 'sell it all' there are situational issues that require answers before such an important decision can be reached:

- Are any of the kids (or grandkids) likely to want to take over the farm operations?
- What happens when the cost to continue outweighs the desire to farm?
- What happens when grain price pressures and paperwork demands become too great?
- What about taxes?
    - Capital gains taxes will take a significant amount from the sale of farmland.
    - Ordinary income tax will be high because there won't be an expense offset if the grain or livestock is sold in a tax year after the expenses were incurred.
- But what happens when it isn't out of a momentary frustration but a longer-term look into the future?

When the farmer talks with his wife (and close partner) about what it would take and what it would be like to, "Sell it all and go sit on a beach somewhere." Their conversation will probably focus upon two things, the kids and taxes.

If their children have all moved off the farm and none of them aspire to take over the farm operation, then selling the farm won't cause an issue with the kids. They could retire and rent out the land and live off the cash rent. They do some quick math and find out that based upon the current land price, their cash rent could be only about 4% per year of the value of their farm.

The thought of selling their farm and losing over 20% of it to capital gains tax and more to ordinary income tax is also not very appealing. So, what do they do?

If the farm family has decided to sell the farm, the following hypothetical scenario can provide insight into deferring ordinary income and capital gains taxes. Farmers First Trust refers to this process as 'Preserving the Value of Your Farm.'

Farmers may refer to this as 'cashing out' but Farmers First Trust calls it 'cashing in.'

Hypothetical Scenario

For our hypothetical scenario, the farm couple live in Greene County Iowa. A center pivot irrigation system was installed in 2009 and their CPA has been depreciating the irrigation system in their tax reporting according to approved tax methods.

They decide to keep the house and buildings but sell 850 acres of tillable farmland. The farmer had inherited the farm from his father years ago, so he has a low basis on his land.

Owned acres: 850 tillable acres
Center Pivot Irrigation: $55,000
Price/acre: $5,050/acre
Total Gross Sale $'s: $4,292,500

Row crop: Corn and soybean rotation
Livestock: No livestock

Machinery: Tractors, combine, planter, sprayer and other equipment, some new and some fully depreciated will be sold at auction. Estimated value at sale could be over $400K.

Buildings: The $340,000 house and 5-acre farmstead will remain in their possession; they will only be selling the farmland and machinery.

Machinery will be sold at auction. The taxable income and associated costs will not be included in our analysis. MDPT does not include depreciated assets.

Decision Criteria

Selling the farm and investing the funds so the farm couple can 'retire on the beach' has now become their objective. One of the largest inhibitors to fully live out their objective, is the capital gains taxes from the sale of the farmland.

Owned acres: 850 tillable acres
****Center Pivot Irrigation***: $55,000
Price/acre: $5,050/acre
Total Gross Sale $'s: $4,292,500

****First Sales Contract***: $55,000 (center pivot irrigation)
****Second Sales Contract***: $4,237,500 (land portion of the sale)
Closing Cost: est. $250,000

Basis per acre: $1005/acre
Basis: $854,250

Exposure to capital gains taxes from land sale: $1,102,245

Tax Type	Marginal Tax Rate	Effective Tax Rate	Tax Amount
Federal	23.80%	23.01%	$778,377
State	8.98%	8.98%	$303,816
Local	0.59%	0.59%	$20,052
Total Capital Gains Taxes			$1,102,245

Greene County Iowa location used for taxes shown.
Numbers shown are for example only and does not represent your tax situation or an actual transaction.
Taxes required for center pivot irrigation not shown.

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!

The farm couple certainly do not desire to send over $1.1M in taxes. They are counting on every dollar to invest and prepare a new life in retirement. Researching MPDT, they discovered that they can defer the $1.1M for up to thirty (30) years before they taxes will be due.

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
Farmland acres sold	850	850**
Net Sale (after closing costs)	$4,042,500	N/A
Depreciated assets on separate sales agreement for MDPT*	N/A	$106,000
MDPT Net Sale amount*	N/A	$3,929,180
Capital Gains Tax Paid (current year)	$1,102,245	N/A
Cash available after transaction	$2,940,255	$3,732,721
Additional cash available with MDPT	N/A	$792,466

See https://www.farmersfirsttrust.com for calculation details.

The MDPT process provides up to 95% of the net sale as cash. The cash received will have interest only payments over the life of the deferred contract. (See https://www.farmersfirsttrust.com for MDPT details.) The net loan cost, as a percentage, could range from 1.4% - 1.6% on an annual basis. The couple discovers that they can have almost $800K in additional funds to invest and live out their lives.

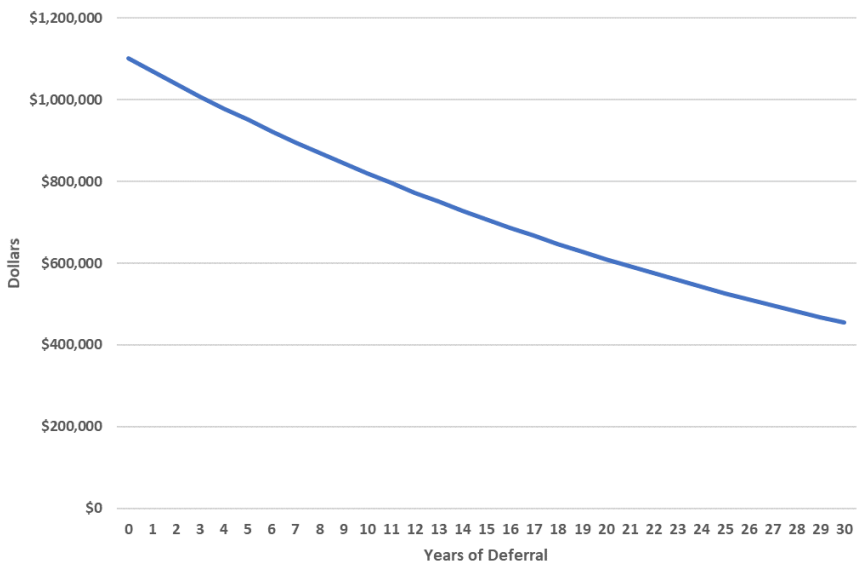
* In this hypothetical example, the center pivot irrigation system is placed in a separate sales agreement as Section 453 does not allow depreciated assets to be involved in an installment sale. MDPT Net Sale amount also includes one-time setup fee cost from Farmers First Trust.

** 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 $1,102,245 we see how the power of present value works in the favor of the farm operation:



Because of time and inflation, $1,102,245 is reduced (comparable to today's $'s) to a little over $454K which is about 59% less than if the taxes were paid in the standard fashion in the year of the sale!

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 heirs.

The example shown created two major financial gains by using MDPT:

- **$792,466** additional cash for retirement/investing/ more than if they were to pay the capital gains tax immediately.
- Deferring **$1,102,245** in capital gains tax for thirty (30) years will be like paying for it with approximately **$454K**, as compared to today's dollars with 3% inflation.

Retain the value of your farm or ranch by using MDPT! By selling the farm, using MDPT this example shows how a retiring farmer can 'cash in.'

Monetized Deferred Payment Transaction MDPT, see **farmers**firsttrust.com for details and background information.

Farmers First Trust Company DST
Offices locations:

101 S Reid ST, STE 307	14 Corporate Plaza, STE 120
Sioux Falls, SD 57103	Newport Beach, CA 92660
(800) 480-8090	(800) 480-8090

farmersfirsttrust.com