The Intersection of Estate Planning & Water Law

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Water Law: An Overview

Background

Water is at the heart of agriculture. The availability of freshwater makes it possible to grow crops and raise livestock. Agricultural water use, in turn, is at the heart of discussions involving water law and policy.

Although water is one of our most plentiful resources, there is often not the right quantity of the right quality of water in the right place at the right time to satisfy demand. Consequently, there is keen competition among water users, including agriculture, municipalities, industry, recreational users, and conservationists.

Agriculture is a major user of ground and surface water in the United States, accounting for approximately 80 percent of the Nation's consumptive water use and over 90 percent in many Western States. Water used in agricultural production is usually sourced from surface waters, such as rivers, lakes, streams, and ponds, or from groundwater stored in aquifers. In some circumstances, agricultural water is also harvested directly from rainfall and stored in above or below-ground cisterns.

Traditionally, management of water resources has focused on surface water or ground water as if they were separate entities. Although water is part of a connected system, it tends to be regulated based upon its source. Even within the category of surface water, water regulations can vary depending on whether the surface water is perennial, ephemeral, or man-made.

Broadly, water law can generally be divided into two substantive areas: rights to use water and restrictions on pollution of water. More specifically, water law concerns: (1) the balance between public rights and private rights to use water; (2) the relative rights of individual water users; and (3) water quality and the regulation of discharges to water. As it relates to agriculture, water law issues tend to fall into two categories: allocation rights and agricultural land use that negatively affects water quality.

Water allocation is generally governed by the states, with each state having its own regulatory system with very little federal intervention. State statutes and regulatory schemes control certain uses of water, such as transfers of water from one watershed to another, withdrawal of groundwater from overused aquifers, impoundment of water, and construction of wells.

Water quality, on the other hand, is governed mostly by federal law, primarily the Clean Water Act.

As the authors point out in their forward to the 5th edition of David H. Getches' *Water Law in a Nutshell:*

A decision to use water for a particular purpose can have far-reaching impacts. For instance, transporting water from a rural area across a mountain range to a city may provide water to sustain the city's population, but it may also force a decline in agricultural productivity and the farming community built on it, facilitate more rapid growth in the importing city, prevent future development of the exporting rural area, curtail recreational opportunities, make sewage treatment more difficult as streamflows to dilute wastewater discharge are diminished, deprive the exporting area of groundwater recharge, and cause ecological changes in both areas. Balancing these conflicting interests and demands is made ever more complex, challenging, and essential in the face of chronic drought cycles intensified by climate change.

It is not surprising then that states have developed and continue to revise legal and regulatory schemes used to prioritize and clarify the relative rights of competing water users.

Private Surface Water Rights

The right to the use of surface waters, whether for irrigation, manufacturing, or another use, is generally governed by state law.

In the United States, three different use allocation systems have developed to determine the rights of private persons in water. The first is the riparian doctrine, which developed in the water-abundant eastern United States. The second is the system of prior appropriation or "first-in-time, first-in-right," that developed in the western United States. Finally, a handful of states have adopted a hybrid system, which contains parts of both the prior appropriation and the riparian systems doctrines. Because water allocation regulation is complex, it is best to contact your state water agency to determine the system used by your state.

The Riparian Doctrine

Riparianism limits the use of water to only those landowners with riparian land. In order to be classified as a riparian landowner, the landowner must own the parcel of land adjacent to the watercourse, i.e. a river, stream, lake, or pond, from which the landowner plans to use the water. Even then, the water may only be put to a reasonable use. The courts can enjoin landowners for unreasonable uses.

The riparian landowner has the right to make "reasonable use" of the watercourse. This means that the riparian landowner may make a reasonable use of the water as long as that use does not interfere with the reasonable use of another downstream riparian landowner. Reasonableness is determined by comparing the proposed use with the other uses of other riparian landowners. Any natural uses, such as water for drinking, watering livestock, or watering a garden, are considered

reasonable under the law. Artificial uses, such as those for irrigation or industry, are considered reasonable uses under most states' laws.

Non-riparian landowners generally have no right to use water, although some riparian jurisdictions may allow it. A majority of jurisdictions require proof of actual harm from the use of water on non-riparian land. The minority follows the Restatement (Second) of Torts § 855, which allows for the reasonable use of water on non-riparian land only if the user also owns riparian land.

Under riparian rights, landowners do not have to use water to keep their riparian rights. New uses may be started at any time as long as the new use is a reasonable one. Because the right is attached to the riparian land, non-use does not extinguish the right.

Today, almost all riparian states have moved towards allocating water through a permitting system, often called a "regulated riparian" system. Under the regulated riparian system, a central state agency controls who may use the water, how much they can use, and when they can use it. Regulated riparianism departs from common law riparianism by looking at the projected use before any water is ever actually used. Using the same "reasonable use" criteria as common law, the states first determine if a new use is reasonable. This allows the state to consider both the potential benefits to society and the compatibility with current uses before granting a new permit. In many cases, the permit is only required on consumptive uses and excludes non-consumptive uses, or uses that do not require a diversion or removal of water from the watercourse.

The permitting system allows the state to plan for and maximize water usage in the future. Even if a use is exempt from a permit, the user may still have to file a water use plan with the state in order to help with planning. However, the rules governing whether a use requires a permit vary from state to state. Further, in many states, agricultural uses are exempt from permit requirements.

Regulated riparian permits exist for a fixed period of years, unlike indefinite permits used in prior appropriation states. In times of water shortages, the state may adjust the quantity of water use allowed and can require a pro rata reduction across the board or based on seniority of use. Permits may also prioritize permitted users over non-permitted users when non-permitted user withdrawals hurt permitted users. Additionally, riparian landowners who do not obtain a permit within the required statutory time period may see a reduction or a forfeiture of their common law riparian rights.

The Prior Appropriation Doctrine

The prior appropriation doctrine dates back to the miners who first settled the West and needed water to develop their mining claims. Because the land needed was not adjacent to a watercourse, the miners could not use the riparian system. Instead, the miners used the "first in time, first in right" system, which was already being used to resolve disputes over water use. This led to the prior appropriation doctrine, where the first user had the right to continue using the water to the exclusion of the rights of those who came later.

The prior appropriation system is based on priority. The most senior appropriator has the highest priority and can defeat all other less senior appropriators in times of shortages. Unlike riparianism, there is no requirement that a senior appropriator use less water in times of a shortage. Water users can take in order of their respective priorities, with each user taking their full appropriative right until the water is gone.

The senior appropriator may enforce his rights by "calling the river." This is a process that allows the senior appropriator to ensure the junior appropriators do not use water out of turn. The senior appropriator will either go to court or the state water agency to have their right enforced against a junior appropriator. If the senior appropriator's water right would be lost through evaporation, instead, the senior only has a "futile call," and the state will not enforce his right against the junior.

The rationale behind this theory is that it is better for water to be used by the junior appropriator rather than lost in transport to the senior appropriator.

The prior appropriation doctrine varies somewhat from state to state, although there are three general requirements: (1) the appropriator must intend to apply water to a beneficial use, (2) the water must be diverted from a natural course, and (3) the water must be applied to a beneficial use. A beneficial use is any use recognized by the state as being an appropriate use of water, such as domestic, municipal, agricultural, industrial and recreational uses. In all prior appropriative states, agricultural uses are considered beneficial uses. The beneficial use is the measure and limitation of the appropriative right. Once water is put to a beneficial use, the right is perfected and has priority over later appropriators. The senior appropriator then has the right to use their original right, even if a "better' use arises later.

In order to have a valid appropriation, an appropriator must show the necessary intent to make an appropriation. The intent necessary is usually just the intent to divert water and apply the water to a beneficial use. In states that require a permit, the application for the permit shows the objective evidence of the necessary intent. A valid appropriation will be given a priority date, or the date the water was first used. Some states have developed the doctrine of relation back that allows the appropriator to use the date that the intent was formed as the priority date.

Historically, the appropriator was required to divert, or build some form of a diversion, in order to provide notice that the water was appropriated. A diversion is typically any alteration to a portion or a stream's entire natural course. In many cases, the capacity of the diversion could be used to determine the extent of the quantity of water appropriated. Today, most prior appropriation states have adopted a permit system that satisfies the notice requirement of a diversion.

Hybrid Systems

Some states, such as California and Oklahoma, have developed hybrid allocation systems, which combine aspects of both the riparian and the appropriative rights systems. While there is no uniform system for all hybrid states, all hybrid systems contain elements of both riparian and prior appropriative rights.

Private Groundwater Rights

Water used in agriculture can also come from underground aquifers. While many groundwater aquifers are connected to surface waters, states' groundwater allocation systems often differ from their surface water allocation systems. Additionally, multiple legal doctrines and combinations of doctrines are used by states to allocate groundwater rights, including the Absolute Dominion rule, Correlative Rights doctrine, Prior Appropriation doctrine, Reasonable Use doctrine, and Restatement of Torts rule.

Groundwater allocation systems often differentiate between on-tract and off-tract uses. On-tract use is where water is used on the tract where the pump is located. Off-tract use is where water is transferred to another location for use.

States often may not fall clearly within a particular doctrine, and may use components of two or more systems. For this reason, it is best to contact your state water agency to determine the allocation system used by your state.

Absolute Dominion Rule

Under the Absolute Dominion Rule, also called the "Absolute Ownership Rule" or the "English Rule," a landowner may use as much ground water as possible. The rule does not take into account impacts on neighboring users, and, as a result, one owner could monopolize the entire aquifer without incurring liability. This doctrine creates an incentive to pump as much water as possible because of the lack of concern of incurring penalties from a neighboring user. Most states have rejected this doctrine, as malicious withdrawals of water could not be enjoined. The states that do continue to follow this doctrine allow for remedies for willful injury. States following this doctrine are Connecticut, Georgia, Indiana, Louisiana, Maine, Minnesota, Massachusetts, Mississippi, Rhode Island, Texas, and Vermont.

Correlative Rights Doctrine

The Correlative Rights Doctrine distributes water on an equitable basis among landowners and allows off-tract uses, although these uses are subordinate to on-tract uses. Like the Absolute Dominion Rule, the Correlative Rights Doctrine determines rights in groundwater based on ownership of land. The difference, however, is that landowners overlying the same aquifer are limited to a reasonable share of the aquifer's total supply, rather than having an absolute right to groundwater or an unlimited right to pump.

This doctrine was first recognized in California in *Katz v. Walkinshaw*, 74 P. 766 (Cal. 1903). The court held that in times of shortages an overlying owner must limit withdrawals to a "fair and just proportion" of the underlying supply. Thus, when two users are both exporting water, the court would use the doctrine of prior appropriation. Finally, in disputes between an overlying landowner and an exporter, the overlying landowner receives a reasonable share of the water, even if the overlying owner is junior to the exporter. The states that apply this doctrine include: Arkansas, California, Iowa, Minnesota, Oklahoma, and Vermont. Nebraska follows a combination of this doctrine and the Reasonable Use doctrine.

Prior Appropriation Doctrine

Many western states have adopted a prior appropriation doctrine for groundwater. Similar to the prior appropriative system for surface water, the first landowner to beneficially use or divert water from a groundwater source is given priority over later users. The right, similar to the surface water system, is limited to the amount that is put to a beneficial use. Many states, today, have replaced this doctrine with a permit system, similar to the surface water permit system. This doctrine is in use in Alaska, Colorado, Idaho, Kansas, Montana, Nevada, New Mexico, North Dakota, Oregon, South Dakota, Utah, Washington, and Wyoming.

Reasonable Use Rule

Some states have adopted the doctrine of reasonable use, or the American rule, which requires the water to be put to a reasonable use on the overlying tract of land and does not permit water to be taken to another tract. Reasonable use has been construed broadly, and almost any use is considered reasonable as long as the water is used on the overlying land. The rule is considered a modification of the Absolute Dominion Rule with exceptions for wasteful uses and off-tract uses. This system is used in Alabama, Arizona, Delaware, Illinois, Kentucky, Maryland, Michigan, Missouri, New Hampshire, New Jersey, New York, North Carolina, Oklahoma, Pennsylvania, Virginia, and West Virginia.

Other states have adopted the reasonable use rule in conjunction with another groundwater rule. Florida has abolished all common law groundwater rights for a permit system, but uses this doctrine in granting permits. Wyoming uses the reasonable use doctrine along with the Prior Appropriative system for groundwater. Nebraska, additionally, uses the reasonable use doctrine along with the Correlative Rights Doctrine.

The Restatement (Second) of Torts Rule

Finally, Ohio and Wisconsin have adopted the Restatement (Second) of Torts approach, which utilizes a variety of factors to determine if a use of water is appropriate. The Restatement's rule is seen as a merger of the Absolute Dominion Rule and the Reasonable Use rule. Section 858 of the Restatement (Second) of Torts states:

Liability for Use of Groundwater

(1) A proprietor of land or his grantee who withdraws groundwater from the land and uses it for a beneficial purpose is not subject to liability for interference with the use of water by another, unless

(a) the withdrawal of groundwater unreasonably causes harm to a proprietor of neighboring land through lowering the water table or reducing artesian pressure,
(b) the withdrawal of groundwater exceeds the proprietor's reasonable share of the annual supply or total store of groundwater, or
(c) the withdrawal of the groundwater has a direct and substantial effect upon a watercourse or lake and unreasonably causes harm to a person entitled to the use of its water.

(2) The determination of liability under clauses (a), (b) and (c) of Subsection (1) is governed by the principles stated in §§ 850 to 857.

Private Water Harvesting Rights

Rainwater harvesting involves capturing, diverting, and storing rainwater from rooftops for later use, including for agricultural irrigation. The practice is not regulated by the federal government and individual state regulations vary widely. Many states do not regulate rainwater collection, or when they do they allow and even encourage it by offering tax credits or exemptions for the purchase of harvesting equipment. Other states, especially prior-appropriation jurisdictions, place restrictions on the amount of rainwater that can be collected and/or the method by which it is collected.

Advances in technology have made atmospheric water harvesting (AWH) (or atmospheric water generation (AWG)) a potentially viable agricultural irrigation tool. Atmospheric water harvesting involves the capture and collection of small airborne water droplets or vapor using sorbents or mechanical refrigeration technology. Fog and dew harvesting are two examples. AWH is not federally governed nor specifically regulated by the States at this time; however, as technology efficiencies increase, the tool is likely to garner regulatory attention.

Public Rights to Water

While agricultural law generally implicates private water rights, it is also important to consider that the public may also have a legal interest in using the water at issue. Public water rights fall under four categories:

- Rights associated with navigation;
- The public trust doctrine;
- Reserved water rights; and
- Public interest protection

Navigation

Navigable servitude is a United States constitutional law doctrine that gives the federal government the right to regulate navigable waterways as an extension of the Commerce Clause. Designed to keep waterways open for commercial navigation, it creates a dominant property right held by the federal government for the benefit of the general public.

Historically, the federal government gave each state ownership of the beds of the navigable waters within the state as part of the grant of statehood. State bed ownership provides another basis for public rights under state law. Federal and state definitions of navigable waters vary considerably, and in many states the public's right to use waters has been expanded to include waterways used for recreational purposes. In 2021, the EPA and Department of the Army announced their intent to review the definition of "waters of the United States." The rule proposed to restore the regulations defining the "water of the United States" that was in place for decades until 2015. Under the final rule, four categories of water are federally regulated

including: territorial seas and traditional navigable waters, perennial and intermittent tributaries to those waters, certain lakes, ponds and impoundments, and wetlands adjacent to jurisdictional waters.

Public Trust Doctrine

The Public Trust Doctrine is a common law doctrine rooted in Roman law that holds that certain natural resources like navigable waters are preserved in perpetuity for the benefit of the public. The state acts as a trustee of the common resource and has an obligation to manage it for the benefit of current and future generations. Attempts by a state to limit or eliminate public trust rights through a sale or by other means may be found invalid.

A number of states have embedded the doctrine in their own constitutions. Traditionally, the public trust applied to commerce and fishing in navigable waters, but in many states its uses have been expanded to include recreation. Notably, states interpret the doctrine and the meaning of public use and public benefit in diverse and shifting ways and, as noted above, also define "navigable waters" or "waters of the state" differently.

Reserved Water Rights

The ability to fully develop water resources through irrigation of croplands or other projects, can be severely limited by federal reserved rights in water. Federal actions reserving public lands implicitly create a water right that allows for enough water to accomplish the purpose of the reservation. Examples include national parks, monuments, and forests, wild and scenic rivers, and Native American reservations. For Native American tribes, the necessary use is the amount of water needed to irrigate all of the tribe's practicably irrigable acreage.

The priority date is the date the reservation is completed. Private rights established prior to the reservation have priority over the reserved rights. The federal right cannot be abandoned or lost through nonuse. Once asserted, it can take water from private right-holders whose rights were established subsequent to the reserved right.

Under the McCarran Amendment, 43 U.S.C. § 666, the federal government has waived sovereign immunity for the limited purpose of adjudicating western water rights. This Amendment authorizes the joinder of the United States in comprehensive stream adjudications, in both state courts and state water agencies. This Amendment has been construed to include the water rights of Native Americans to reduce the number of court proceedings to determine the same rights. The Amendment allows for the more efficient adjudication of water rights along streams in the Western States.

Public Interest Protections

Some states statutorily mandate public interest review of initial water right allocation or increases, requiring an appropriation permit from an administrative agency and allowing the permit to be issued only if the proposed appropriation conforms to the public interest or public welfare.

Historically, public interest criteria were satisfied if the permit applicant would benefit economically from the water use. More recently, public interest criteria are expanding to include environmental and other public concerns, requiring consideration of the cumulative effects of water withdrawals from ground or surface waters. Similar protections include state statutes creating minimum streamflow requirements or authorizing instream flows.

Water Pollution

Water pollution law is extraordinarily complex. It can involve areas of common law such as nuisance, trespass, and negligence, but more often it involves an interconnected network of federal and state statutes and regulations, the cornerstone of which is the Clean Water Act (CWA). A partial list includes laws regulating surface water discharges from point sources; sedimentation and erosion; stormwater runoff; land uses in nutrient-sensitive waters and water supply watersheds; and sources of groundwater pollution. Federal regulatory programs also include regulation of wetlands and construction in navigable waters and establishment of total maximum daily loads in highly polluted surface water bodies.

As described on the US Environmental Protection Agency website:

The Clean Water Act provides a comprehensive system for the regulation of pollutants in the waters of the United States with the objective of restoring and maintaining the chemical, physical, and biological integrity of the nation's waters. The CWA operates by authorizing water quality standards for surface waters, requiring permits for point source discharges of pollutants into navigable waters, assisting with funding for construction of municipal sewage treatment plants, and planning for control of nonpoint source pollution.

The Environmental Protection Agency ("EPA") is the primary agency tasked with implementing and enforcing the CWA, although the agency can and does delegate permitting authority to individual states.

FARM TRANSITION AND ESTATE TRANSITION PLANNING: WHAT IT IS AND WHAT TO EXPECT

Pick up a farm magazine and it's likely to have an article about estate planning. An internet search will yield hundreds of references to passing on the family farm, protecting a farm's legacy, and bringing the next generation into the operation. We focus a lot of attention today on farm transition and estate planning. That's because good planning carries critical consequences for the future of agriculture.

WHAT IS FARM TRANSITION AND ESTATE PLANNING?

Farming is both a unique way of living and a unique way of making a living. It is common for farmers to hope to pass this unique heritage on to future generations. "Farm estate planning" uses legal tools to ensure that the next generation receives farm assets after farm owners retire or pass on. But farmers often want to bring their heirs into the farming operation before passing those assets on. The term "farm transition planning" refers to using many tools to prepare for and transfer the farming operation to heirs, including estate planning and business planning tools. Whether your goals are to pass on land and assets, hand the farm business down to future generations, or both, learning about farm transition and estate planning will help you accomplish those goals.

THE FARM TRANSITION AND ESTATE PLANNING PROCESS

The farm transition and estate planning process begins with **identifying goals** for the future of the farm and the farm family. We frequently hear from farmers whose primary goals are to keep farmland in the family and prepare the next generation of managers. Or perhaps a farmer aims to retire, address special issues with children, or plan for long term health care. Whatever the goals may be, healthy **family communication** and **conflict management** are often necessary to accomplish this important first step of identifying goals.

This work is supported by the National Agricultural Library, Agricultural Research Service, U.S. Department of Agriculture. It is provided for educational purposes only, is not legal advice, and is not a substitute for the need to consult with a competent attorney licensed to practice in the appropriate jurisdiction.

The next step in the farm transition planning process requires **selecting strategies** to implement established goals.

Strategies will likely be necessary in several different areas:

- **Human resource** strategies to identify, prepare and train the next generation of the farm business managers.
- **Financial** tools to aid in funding and implementing goals, such as insurance and retirement plans.
- **Legal** strategies and tools for effective asset protection and transfer, such as estate planning and business planning instruments.

The Farm Transition Planning Process

The legal tools and strategies component of farm transition planning is the focus of our Planning for the Future of the Farm bulletin series. Some of the legal tools we explain are traditional instruments often used in estate planning, like wills and trusts. But other legal tools can be useful for a farm transition plan, such as business entities, operating agreements, leases, and gifting strategies. These legal tools work together with human resource strategies and financial tools to implement a farm's goals. Putting the legal plan in place is the final step in the farm transition planning process.

PUTTING A LEGAL PLAN TOGETHER

1. Choose an attorney. The legal side of farm transition planning starts with choosing your attorney. Word-of-mouth is one way to identify a good agricultural attorney with expertise in farm transition and estate planning, or check with organizations like Extension, the state or local bar association, or the American Agricultural Law Association. Ask for an initial consultation and meet an attorney before committing to representation. Several factors can aid in selecting the right attorney: competence, personal comfort, and costs.

- Look for an attorney with **competence** in estate and business planning—composed of both legal knowledge and practical experience. But don't stop there-- it's also very important that the attorney is competent with **agriculture** and experienced in working with farm clients. Farm businesses are different than other types of businesses. An attorney who knows farming will have insight into the laws, tools and strategies that apply to farm situations. Be wary of an attorney who has never worked with farm clients and knows little about agriculture.

- **Personal comfort** with an attorney is essential. It can ensure open communication and make it easier to share necessary information about finances, assets, business plans, and family issues and dynamics. Discomfort can lead to misunderstandings, withholding of critical information, and plans that don't align with a family's goals.
- **Costs** can vary. It is completely acceptable to request an estimate of legal fees. Don't be afraid to ask what the entire plan, from start to finish, will cost.

2. Expect to have two or more meetings with an attorney. The first meeting is typically for reviewing goals and information but might also involve discussing strategies and options. Additional meetings could involve reviewing tools and strategies and executing legal documents.

3. Prepare for the first meeting. Advance preparation can help the first meeting move more efficiently and effectively. An attorney might let you know in advance of information to gather before the first meeting. Also consider these tips:

- **Write it down.** Write out your goals for the farm business and farm assets. Also include information about the family, its special needs, and its dynamics. Consider details an attorney may need to know about the farm and the family, like who has "sweat equity" in the business, siblings who don't get along, children with problems managing finances, big purchases coming up, and who wants to be involved in the farm—this and similar information will help with developing a plan that addresses future issues.
- **Compile asset and personal information**. Gather all asset information such as deeds, account numbers and balances, and beneficiary designations, along with personal information on you and your family members. OSU Extension offers a helpful document, Getting Your Farm and Family Affairs in Order, that can aid in organizing the information. Doing so before meeting with your attorney can save time and the costs of having your attorney track down the information.
- **Organize financial information**. Use the information gathered in step two to prepare a simple balance sheet showing farm assets, non-farm assets, debts, and net worth. Full disclosure of your financial situation is necessary to developing a plan that addresses financial challenges and opportunities and is another way to save on the costs of paying your attorney to compile the information.

4. You may need your other advisors, too. Communication among all your professional advisors may be necessary to ensure all strategies align with one another. You may need to check in with financial advisors, accountants, insurance agents, and other professionals you rely upon.

SPEAKING THE FARM TRANSITION LANGUAGE: COMMON TERMS

Farm transition planning uses many legal terms, and familiarization with the terms should help you through the process. Here are definitions to common terms you may encounter along the way.

Advance directive. A legal document that gives instruction on a person's health care wishes, such as a living will and health care power of attorney.	Irrevocable trust. A trust that cannot be changed or cancelled by the person who executed the trust.

Basis and step-up in basis. The basis is the value of an inherited asset for tax purposes. A step-up in basis is an adjustment of basis to the asset's fair market value at the time of the death that triggers the inheritance.	Joint tenancy. Ownership of real property jointly by two or more parties, either as joint tenants with rights of survivorship or as tenants in common.
Beneficiary. A person designated to receive proceeds from an asset such as an account, insurance policy, or trust upon the death of the owner of the asset.	Living trust. A trust created during a person's lifetime to manage assets before and after the person's death. A living trust can be revocable or irrevocable.
Business entity or structure. An organization formed to conduct business, such as sole proprietorships, partnerships, corporations, cooperatives, and limited liability companies.	Living will. A legal document stating a person's wishes for medical treatment and life-sustaining measures if the person is at the end of life and unable to communicate.
Capital gains tax. A tax on the increase in the value of an asset between the time it is bought and the time it is sold.	LLC, Limited Liability Company. A business entity that can protect its owners from personal responsibility for business debts and liabilities with pass-through taxation.
Deed. A written document that transfers title to real property to a new owner.	Long-term care insurance. Insurance coverage for long-term services and support not covered by health insurance, such as nursing home or custodial care.
End-of-life directive. A written legal document with instructions for end-of-life medical decisions if a person is unable to make decisions at that time.	Operating agreement. A document that governs the internal operations of a limited liability company and is binding on all members of the limited liability company.
Estate. All of the real and personal property a person owns at death.	Payable on death account. An account set up to be directly transferred to a beneficiary upon the death of the account holder, without going through probate.
Estate administration. The process of collecting assets, paying debts, and distributing the property of a person after the person's death.	Probate. A court process to administer a person's estate by paying all claims, expenses, and taxes, and distributing remaining property to heirs.
Federal estate tax. A tax on the portion of a person's estate that exceeds the federal estate tax exemption amount.	Revocable trust. A trust that can be changed or cancelled by the person who executed it prior to that person's death.
Federal estate tax exemption. An amount of assets in an estate that are exempt from the federal estate tax, as determined by Congress and adjusted annually.	Survivorship deed. A deed that transfers the title to a joint owner's share of jointly owned real property upon death to the surviving joint owners.
Financial power of attorney. A legal document that appoints someone to make financial decisions for a person if the person is unable to manage their finances.	Tenancy in common. A form of joint ownership of real property that allows a joint owner to transfer their share of property to a person other than a joint tenant.
Gifting. Giving cash or assets to a beneficiary during the giver's lifetime rather than after death, which can reduce the value of the giver's estate and the possibility of estate taxes at death.	Transfer on death affidavit. A written instrument that establishes a direct transfer of real property to a designated beneficiary upon the death of the owner without going through probate administration.
Health care power of attorney. A legal document that allows an individual to empower another person to make important medical decisions on their behalf when they cannot do so themselves.	Trust. A legal instrument that holds assets and appoints a trustee to oversee and distribute assets according to the terms of the trust.
Intestacy. Dying without a will, which results in the deceased's assets being subject to probate and distributed according to the state's intestacy law.	Trust administration. The process of managing the assets within a trust according to the terms of the trust.

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Find all our **Planning for the Future of Your Farm** resources at https://go.osu.edu/farmplanning

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WILLS AND WILL-BASED FARM TRANSITION PLANS

Your will, or "last will and testament," is one way for you to determine what happens to your property after your death. A will is a necessary part of a farm transition or estate plan, but how it is used can vary widely. Some plans may need only a will in conjunction with a few simple tools—we refer to these as "will-based plans." Other plans, however, may be more complex and require additional legal tools. We explain wills and their role in farm transition planning in this bulletin.

WILLS SERVE MANY PURPOSES

The "reading of the will" after someone dies can be a dramatic event, with family members wondering what the will says and who gets what. Distributing property is just one purpose of a will, however. A will can have several helpful purposes, explained here.

Determining where property goes. A will transfers property after death according to a person's wishes. The terms of a will can be quite specific about how property passes. It can include restrictions and conditions tailored to the deceased person's wishes and can "disinherit" heirs that otherwise would receive property if the person did not have a will. A will can also include alternative plans in the event of changed conditions and circumstances.

Minimizing the probate process. A will sends clear directions to the probate court. Without a will, the court would otherwise have to determine how property should pass according to law. And as we explain later, a will can direct property to an existing trust and reduce the need to transfer it through the probate process. Both actions can reduce the time spent in probate, as well as the costs.

Choosing who administers the estate. A person can appoint an **administrator** to help settle the person's estate. The administrator, also called an executor or personal representative, will help resolve the deceased person's financial affairs and carry out the directives in the will. It is an important role, so it's critical to choose an executor carefully.

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Naming guardians. One critical role a will can play is to address who will care for dependents such as minor children and incompetent adults upon the death of their caretakers. Parents or other persons with dependents may nominate a guardian in the will, and the court will review that nomination when appointing a legal guardian. The will may also specify whether the guardian is to manage the dependent's personal needs, property, or both.

WHAT IF YOU DON'T HAVE A WILL?

Every state in the U.S. has an "intestacy law" or "statute of descent and distribution" that steps in when a person dies without a will and directs distribution of the person's property. As with other states, Ohio's intestacy law makes assumptions that the deceased would choose to give property to family members. The law establishes an order of preference that gives a surviving spouse first priority, then children of the deceased and their children. If there is no spouse or children, the law looks next to parents, then to other family members. The State of Ohio receives the property if there are no family members. Ohio law also gives the probate court authority to appoint an administrator to assist with settling the estate of a person who dies without a will.

THE FORMALITIES OF MAKING A WILL

Requirements for making a will are straightforward but failing to meet them can result in a will being declared invalid. A person must be 18 years or older to make a will and be of "sound mind and memory" and "not under restraint." These terms mean that a person must know what he or she is doing and that making the will is a free and voluntary act. A will must be in writing, although it need not be typed, and the person making the will must sign it or if unable to do so, direct someone else to sign in their presence. Two or more witnesses must acknowledge that the person made and signed the will and must also sign the will in the presence of the person making the will.

Many "fill-in-the-blank" wills are freely available, but we advise working with an attorney to develop a will. Doing so will ensure not only that the legal requirements for making the will are satisfied, but more importantly that the will properly fits with the farm transition plan.

DIFFERENT TYPES OF WILLS

How a will distributes property can vary. A will can direct property to an identified party, send property to an established trust, or order a trust to be set up to receive the property. Here's an explanation of these three different types of wills:

A **simple will** directs all property to a surviving spouse or if the spouse is pre-deceased, then to the children. A simple will might also make specific bequests of property, name an executor, and appoint a guardian for minor children. The "simple" name for this type of will means that it does not involve a trust, making it less complex than wills that do. Some call this type of will a "sweetheart" will, because the plan is to leave all or most of the property to the deceased's sweetheart. The sweetheart then determines the fate of the property at his or her death.

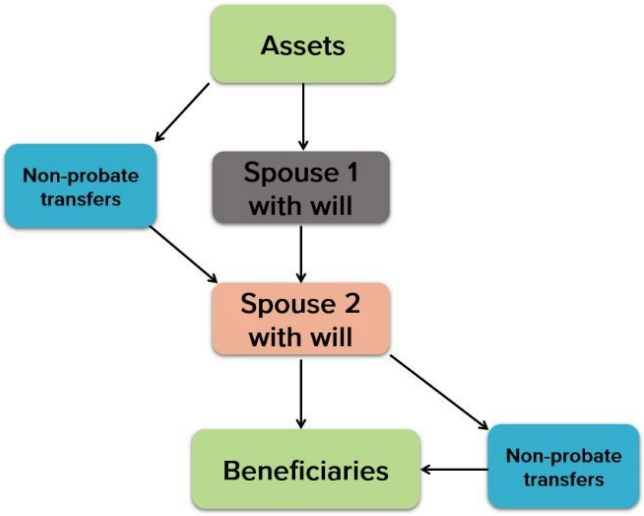
A **pour over will** transfers property to a "living trust" that was created prior to death. The assets "pour over" into the trust at death and the trust provisions then control what happens to the assets. This type of will is an important part of a trust-based plan and ensures that all property goes directly into the pre-existing trust rather than through the probate process.

A **complex will** directs the creation of a trust after death, referred to as a "testamentary trust." A testamentary trust might be simpler than a "living trust" and might only arise if certain conditions exist at death. For example, a simple testamentary trust could direct assets into a trust to support minor children if both parents pass. The trust only arises if the children are minors and both parents are deceased. Because a will creates the trust, the probate court would oversee administration of the trust by the trustee named in the will.

A WILL-BASED FARM TRANSITION PLAN

A plan can use a simple will to pass assets from one spouse to the next and then on to heirs. Other tools might be involved in the plan, such as transfer on death accounts, which we explain in our bulletin Legal Tools for Avoiding Probate. But the plan doesn't require the use of a trust. We refer to this approach as a **"will-based plan."** The illustration to the right shows how a will-based plan combined with non-probate tools can transfer farm assets to the intended beneficiaries. This approach can be sufficient for many people, but most often doesn't work well to address the complexities and assets of farm families and transitioning farm businesses.

A simple will-based plan



DO YOU ALSO NEED A TRUST?

Can you accomplish your plans for the future with a will-based plan? Or do you need a trust-based plan that uses a trust to help carry out the transition of your farm and assets? Those are "it depends" questions, as several factors come into play. The complexity of your situation is probably the critical factor that could lead you to a trust-based plan rather than a will-based plan. For example, if you have heirs with special needs, want to place certain conditions on heirs receiving property, need to address details ensuring transition of the farm to a specific heir, or are worried about federal estate taxes, a will-based plan may not be able to address your needs.

Likewise, you might prefer a trust because you want to avoid probate court involvement and have a trustee in charge of administering your affairs. You may also prefer to place details in a trust because of the privacy it offers in comparison to a will, which becomes an accessible public record when it goes through probate. Finally, legal fees are a factor. While a trust-based plan will likely cost more to create at the outset, it can keep assets out of probate and save on probate fees. A will-based plan is probably less expensive to create but could result in higher costs if assets must transfer through the probate process.

In the chart below, we outline how different factors play out in will-based versus trust-based plans. Discussing the factors with family and an attorney can be helpful. To learn more about trusts and using a trust-based plan in farm transition planning, see our other bulletin in this series, Using Trusts in Farm Transition Planning.

Comparing a will-based plan with a trust-based plan

Factor	Will-based plan	Trust-based Plan
Complexity of situation	Simple	Complex
Concerns about heirs	Little or none	Some or significant
Remarriage concerns	Little or none	Some or significant
Transition of operation	Little or none	Some or significant
Estate taxes	Little or none	Need to maximize savings
Probate	Don't mind; judge is in charge	Want to avoid; trustee is in charge
Privacy	Not important	Important
Cost	Less at outset; maybe more later	More at outset; maybe less later

UPDATING A WILL

How often should you update your will? It's important to be aware of circumstances that can trigger the need to review and update your will. Major life events are the most common triggers, including:

- Marriage, remarriage, or divorce in the family
- Birth of a child or grandchild
- Death of a spouse or beneficiary
- Change in health status
- Inheritance or other income that affects the value of your estate
- Moving to a different state
- Estate or tax law changes

WORKING WITH AN ATTORNEY

Many "fill-in-the-blank" wills exist but be wary of the one-size-fits-all approach they offer. An attorney plays an important role in developing a will that not only expresses your wishes but also addresses contingencies, considers the estate and tax laws that govern your estate, and fits the will into the overall farm transition plan. See our resources on choosing an attorney and talk with friends and family to find an attorney who will help you with the important task of creating a will that can carry out your plans for the future.

REFERENCES

Ohio Revised Code Section 2105.06, Descent and distribution https://codes.ohio.gov/ohio-revised-code/chapter-2105

Ohio Revised Code Chapter 2107, Wills https://codes.ohio.gov/ohio-revised-code/chapter-2107

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USING TRUSTS IN FARM TRANSITION PLANNING

Maybe you've asked the question, "should I have a trust?" It's a common question for farm families who are planning for the future of the farm. Trusts have become quite popular, with good reason. Trusts can be useful tools for keeping farmland in the family, avoiding probate, holding assets for minors, and more. But while a trust may have many applications and benefits, it may not always be the right solution for your farm transition goals. A careful analysis with your attorney and professional advisors is the best way to determine whether you need a trust. This bulletin offers explanations of trusts and illustrates roles they can play in farm transition planning.

WHAT EXACTLY IS A TRUST?

A trust is one of several tools that holds and transfers assets. Think of a trust as a container. You can place your assets in the container at any time—during life, immediately upon death, and after death. You can create terms and conditions in the trust. Then the assets are distributed out of the trust by the trustee according to the terms and conditions.

To help understand how a trust works**, consider the following example:**

Andy establishes a trust for his land and includes the following provision: "Upon my death, my son Bill shall have the option to purchase the land. The purchase price shall be 75% of the land's appraised value. My trustee shall provide Bill written notice of his option to purchase the land within 60 days of my death. The purchase proceeds shall be distributed to all my children equally."

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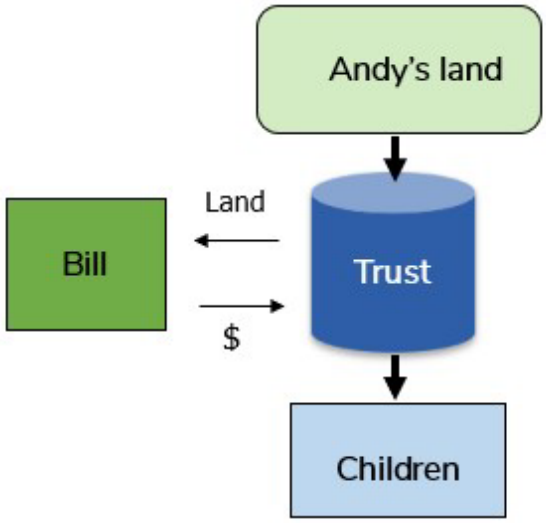
In this example, after Andy's death, his assets will be held in his trust and eventually distributed to out to his beneficiaries. While the assets are in the trust, the trustee will administer the terms and conditions of the trust as established by Andy prior to his death. Here's how the trust could play out:

1. The land goes into Andy's trust upon his death.
2. The Trustee provides Bill written notice that he has the option to purchase the land at 75% of appraised value.
3. Bill elects to buy the land and pays the purchase price to the trust.
4. The trustee distributes the purchase proceeds to all of Andy's children.



As the example shows, the trust is the container that holds Andy's assets. While the assets are in the trust, conditions can be placed on the assets which the trustee must enforce. Ultimately, after the conditions of the trust have been met, the assets flow out of the trust to the trust beneficiaries.

There are essentially no limits to the type and number of conditions that can be placed on assets as they flow through a trust. The conditions in the trust can be very simple, such as giving a beneficiary the right to buy an asset, to very complex, such as holding assets in the trust for multiple generations with restrictions on how the assets can be used. One of the key benefits of a trust is the flexibility it provides for planning because conditions can vary so widely.

HOW LONG ARE ASSETS HELD IN TRUST?

How long it takes from the time assets go into a trust until they leave the trust depends on a trust's conditions and purposes. Sometimes assets transfer through the trust within a few days, weeks, or months. Other times, assets may remain in a trust many years before being distributed.

Assets held in the trust only a short period of time may be assets needed by the next generation to continue farming. Holding assets such as machinery and livestock in trust may impede the ability of the next generation farmer to effectively operate the farm. **Consider the example on the following page:**

George is a farmer who owns farm machinery. Mary is George's daughter and the successor to the farming operation. George's trust provides that all farm machinery is to be distributed outright to Mary. George dies just as planting season is starting and Mary needs to use the machinery. The trustee distributes the machinery to Mary immediately so that Mary's farming operation is not interrupted.

As this example shows, it is possible for some assets to be held in trust only a few days. Because the machinery is to go directly to Mary with no additional conditions, the trustee is free to distribute out the machinery very quickly.

We pointed out above that assets can also stay in a trust for many years. Often, real estate is the most common asset to be held in trust for a long period. Farmers will sometimes require their land be held in a trust for an entire generation to keep the farmland available to future generations. **Consider the following example:**

George's land has been in his family for five generations. He does not want the land sold until his grandchildren have a chance to farm it. He establishes a trust with the following provision: "All of my farmland shall be held in trust for the benefit of my children. While the farmland is held in trust, my daughter Mary shall have the option to lease the land. Upon the death of all my children, the farmland shall be distributed to my grandchildren. At the time of distribution, any of my grandchildren who are actively farming shall have the option to lease the land."

In this example, the farmland will be held in trust for the lifetimes of George's children. Perhaps the land is held in trust for as long as 50 years. This is a perfectly acceptable way to use a trust.

As this discussion demonstrates, trusts can be used to hold assets just long enough to transfer them to a beneficiary or to hold assets for many years to meet the goals of the grantor. When considering the use of a trust, the amount of time that the assets will be required to be held in trust is an important consideration.

TRUSTS AND PROBATE AVOIDANCE

A primary characteristic of a trust is probate avoidance. Probate is a time-consuming process. It can take months or longer to administer an estate through probate, but a trust continues to operate without having to wait on probate. Probate can also be expensive.

As we discuss in our other bulletin in this series, Legal Tools for Avoiding Probate, we can avoid probate of titled assets without the use of a trust with payable-on-death or transfer-on-death designations. These assets include financial accounts, life insurance, vehicles, and real estate. But

non-titled assets such as equipment, crops, grain, and livestock can only avoid probate by using a trust. Farms with substantial amounts of these non-titled assets can keep those assets out of probate by using a trust. **Consider the two scenarios in the following example**:

Scenario 1. Jane owns a large inventory of farm machinery. For her estate plan, she has a simple will leaving the farm machinery to her children. When she dies, the machinery will be subject to probate. It will likely take several months, at a minimum, to complete the probate process to transfer the machinery to the children. Additionally, considerable legal fees will be required to file the appropriate forms with the probate court.

Scenario 2. Jane elects to have a trust for her estate plan. When Jane dies, the machinery will be in her trust. Jane's trustee can distribute the machinery to Jane's children at any time after Jane's death. Other than perhaps a simple document recognizing the children's receipt of the machinery, the machinery can pass to the children with little effort and in a short amount of time.

This example highlights the probate-avoiding benefits of a trust. For farm operations with large inventories of machinery, livestock, grain, crops and other non-titled assets, trusts will usually save significant time and legal fees by avoiding the probate process.

DO YOU NEED A TRUST?

A trust is not necessary for every situation; sometimes a simple will is adequate. Several factors can help with deciding if the benefits of a trust outweigh the extra costs and complexities of a trust. The following are a few of the more important factors to consider when making this decision.

1. Complexity of plan

Generally, the more complicated the plan the more likely a trust is the better option. Remember that assets that are subject to a will are also subject to probate court oversight. While probate courts provide an important service and do a good job of administering many estates, the probate process is also well known for being laborious and time consuming. Administering a complicated plan through a will and probate can get bogged down very quickly.

A trust is not subject to probate oversight. The trustee administers the trust with the oversight of only the beneficiaries. The administration of assets through a trust can often be done much more efficiently and quickly than probate. Trust administration does not have all the constraints and formality of probate. **Consider the following examples**:

Example 1. Mike's goal is to have his farmland go to his three children equally with no additional conditions. A trust is likely not needed as the distribution plan is simple and straightforward.

Example 2. Mike would like all three of his children to benefit from his farmland. However, he wants his son Nick to have the option to purchase the other children's ownership interests. He also wants to set the purchase price at 80% of the appraised value and give Nick 10 years to pay for the land at the lowest allowable interest rate. A trust is likely the better option for this scenario because of the complexity involved with Nick's option to purchase. While this scenario could be done through probate, it would take much longer and likely incur significant legal fees. Instead, by using the trust, the trustee obtains an appraisal, makes the offer to Nick and collects the sale proceeds – all without the need to involve the probate court.

The more complex the estate plan becomes, the more likely a trust is the better option. Wills are the better option for people with simple plans, but most farmers do not have simple plans. Farmers often include options to purchase, leases, rights of first refusals, and many other complicated components in their plans. For many farmers, a trust will be the better option for their estate plan.

1. Transition of operation

One of the primary concerns of many farmers is the transition of the farming operation to the next generation. Trusts can allow the farming operation to flow to the next generation farmer quickly and efficiently. This quick and efficient transition can help ensure that the farming operation remains viable and profitable for the successor farmer. **Consider the following example:**

Linda owns a herd of beef cattle. Her intention is for her two children to inherit the cattle. Linda knows the cattle should be sold upon her death since her children have no interest in the cattle and have never helped with the cattle. Linda dies unexpectedly a week before her cows are to start calving.
Scenario 1. Linda dies with only a simple will that leaves everything to her children. Before the cattle can be sold, Linda's estate must be opened in probate court and an executor must be appointed by the court. Then, the executor must receive permission from the court to sell the cows. This process could take several weeks and in the meantime, the cattle have likely started to calve and there is no one to take care of the cattle or the new calves.
Scenario 2. Linda had set up a trust before her death which holds the cattle. Upon Linda's death, the trustee is able to immediately find a buyer and sell the cattle. All the cattle are sold to another beef operation before they begin calving.

This example shows how a trust can provide a better transition of the farming operation. In the first scenario the probate court was required to be involved, which could hold up the transition. In the second scenario the trustee had the authority to sell the cattle immediately upon Linda's death. The independence enjoyed by the trustee allows decisions to be made faster and actions to be taken quicker–both important to a smooth transition of the farming operation.

3. Concerns about heirs

Most people want to leave an inheritance to their heirs to help improve their lives and the lives of future generations. But sometimes, there may be concerns that the heir may not be able to manage the inheritance left to them or that it may be lost to frivolous spending or creditors. A trust can help ensure that an inheritance will be protected from mismanagement or loss.

A trust strategy uses a trustee to manage an heir's funds. The trustee can provide the heir with income and/or principal from the trust and can also limit the resources available to the heir to be sure it is not wasted. The assets can be held in trust until certain conditions are met, for a certain period, or for the life of the heir. **Consider the following example:**

Nancy wants to leave her farmland to her two children, Paul and Oscar. Paul has never been able to manage his finances and spends every dollar that is available to him. Nancy is concerned that if Paul inherits the land he will immediately sell it to get money to spend on things he does not need. Nancy wants Paul's children to be able to enjoy and benefit from the land someday.

Nancy establishes a trust. Upon her death, Paul's share of the land will be held in trust for the remainder of his life. Oscar, who is responsible and good with money, will be the trustee of Paul's trust. Oscar will manage the land on behalf of Paul and will release only the income generated from the land annually to Paul. The trust instructs Oscar not to sell the land and upon Paul's death, to distribute the land to Paul's children.

When facing a scenario in which the heir should not receive the assets directly, a trust is an excellent means to protect the assets. This strategy can be used to protect assets from issues that heirs may have such as drug/alcohol abuse, gambling, creditors, lawsuits, bankruptcies, spending problems, and marriage problems. Wills, conversely, provide limited options to protect assets for heirs.

4. Estate taxes

In the last decade, federal estate taxes have become less of a problem for farmers because the federal estate tax exemption has steadily increased. And many states, like Ohio, no longer have estate taxes. This means only a small fraction of farm families face the prospect of paying estate taxes. However, for those farm families who do face estate taxes, trusts are a near necessity.

A discussion on the intricacies and complexities of estate taxes and trusts is beyond the scope of this publication. However, it can safely be said that trusts provide opportunities to reduce estate taxes that cannot be accomplished by a will alone. This estate tax savings benefit is mostly applicable to married people because assets can be held in trust at the death of the first spouse. For unmarried people, trusts do little to reduce estate tax liability and thus a will may be an adequate solution.

5. Privacy

The process of probate is overseen by a probate court and all filings and information are open to public access. For some people, the idea of having information about their will, assets, and heirs be publicly available is not a big concern. For others, privacy is a priority.

Trusts can maintain privacy. Because a trust is a private document and only the trustee and beneficiaries are entitled to see it, a person's assets, beneficiaries, and distribution plan remains completely private. For individuals who wish their estate information to be private, a trust is a better option than a will.

6. Legal fees

Generally, trusts are more complex legal documents than wills and usually cost more in legal fees, although costs vary greatly from one attorney to another. However, the attorney and probate fees for implementing a will-based plan can be several times more than the costs to administer a trustbased plan. Before engaging an attorney to draft a will or a trust, be sure to understand what the total costs will be as this is an important factor in deciding between a will or trust.

OTHER BENEFICIAL CHARACTERISTICS OF A TRUST

There can be other benefits of incorporating a trust into your farm transition plan. We explain these additional benefits and considerations below. If any of these are important to your goals for the future of your farm, consider using a trust to accomplish those goals.

Control after death. A trust allows you to continue to control the assets after your death through the terms of the trust. For example, the trust could hold farmland after death and not allow that farmland to be sold for 50 years or more.

Planning for second marriages. In a blended family involving a second marriage after the loss of a first spouse, a trust can provide income and support for your second spouse if you pass away while keeping farm assets in your family. If your second spouse later remarries after your death, the trust could direct the assets to go to your children, whether from the first or second marriage, and the assets won't end up in your second spouse's new family. This strategy can keep farmland and other farm assets in your family in a second marriage situation.

Restrictions for minors. A trust can include provisions requiring your children to meet certain age requirements before they receive income from an asset or the asset itself.

Provide for heirs with special needs. Much like a trust can provide for a surviving spouse, a trust can manage funds and assets for loved ones with special needs like a handicap or disability who might not be able to care for themselves after you pass away. Appointing a trustee to manage the assets and income for your beneficiary gives you the assurance that your loved one will have the funds and care needed to live a comfortable life.

Giving to charities. In addition to providing for loved ones, you can also use a trust to support your passions. You can establish a charitable trust that names certain charities, or you can describe causes or issues you want to support with the trust assets.

GIVE CAREFUL CONSIDERATION TO TRUSTS

Trusts are valuable tools for farm transition planning. However, trusts are not necessary for every plan. Consider the benefits of a trust to determine if it is the best asset transfer tool for you. Your estate planning attorney can help guide you through the process.

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