

Some farm estate plans spend years trying to reduce a tax bill that may never come due—and overlook a tax bill that could show up as soon as the family sells equipment, land, or a business interest. That is the difference between planning for estate tax and planning for income tax. They are separate systems, and a strategy that helps with one can create trouble in the other.

For many farm families, estate tax exposure is rare, while income tax is a more immediate succession threat. Depreciation, asset sales, installment payments, and the tax basis of inherited property can all affect what heirs actually keep. A plan that names successors but ignores those details can leave the next generation with a large tax bill and too little cash to pay it.

Before discussing any strategy, ask: **Who is likely to sell this asset, and when?** The answer can matter more than the size of the estate on paper.

Estate tax and income tax are not the same problem

Estate tax generally concerns the transfer of wealth at death. Income tax applies to income and certain gains during life or after death. Farm families often use “estate tax” as shorthand for any tax connected to a death or inheritance, but that can lead them to miss the actual tax rules involved.

Estate tax exposure is uncommon for most farm estates, though a particular family may have reasons to examine it closely. The value of land, equipment, buildings, life insurance, and other assets can add up, and laws and exemptions can change. Families should confirm their situation with qualified advisers rather than assume they are either protected or exposed.

Income tax can affect a much broader range of farm families. It can arise when a farmer sells an asset, when a business distributes property, or when heirs later sell what they inherited. A farm may have substantial wealth tied up in land and equipment but limited cash available to cover a tax bill. That mismatch makes income tax a practical succession issue, not just a technical one.

The farm succession planning mistake: planning only for the transfer

A succession plan often focuses on who receives the farm, who gets voting control, and how non-farming heirs will be treated. Those are important questions. But naming a recipient does not tell you what that person’s tax basis will be, whether depreciation has reduced it, or what happens if the recipient sells the asset.

This is a common **farm succession planning mistake**: treating the transfer itself as the finish line. In practice, the transfer may be followed by a sale, refinancing, buyout, or change in how the asset is used. Each choice can have different tax consequences.

For example, a farming child might keep using machinery for years, while a sibling who inherits a share of the business may want a cash buyout. If the plan assumes everyone will hold the same assets indefinitely, it may fail the moment someone needs liquidity.



Depreciation can make paid-off equipment a tax problem

Farmers commonly depreciate qualifying equipment and other business property over time. Depreciation can reduce taxable income in the years it is claimed, but it also reduces the property's adjusted tax basis. The basis is generally the starting point for measuring gain or loss when an asset is sold.

That creates an easy-to-miss gap between what equipment is worth and what its tax basis is. A tractor may be fully paid off and agdaily.com still have substantial market value. But if the farmer has claimed most or all of its tax depreciation, the adjusted basis may be very low. Selling it for more than that basis can produce taxable gain.

For certain depreciable business property, including much farm equipment, **IRC Section 1245** can require depreciation recapture. In broad terms, gain on a sale may be treated as ordinary income up to the amount of depreciation previously allowed or allowable, subject to the statutory rules. Ordinary income can be taxed differently from capital gain. The exact result depends on the asset, its basis and depreciation history, the sale price, and the transaction details.

"Paid off" describes the debt. It does not describe the tax basis. A machine can be debt-free but still carry a significant potential tax cost if the owner sells it.



A simple illustration

Suppose a farmer bought a piece of equipment for \$100,000 and claimed \$80,000 of depreciation. For a simplified illustration, assume its adjusted basis is \$20,000 and it is later sold for \$70,000. The sale creates \$50,000 of gain before considering transaction-specific rules. Some or all of that gain may be ordinary income under Section 1245, up to the applicable recapture amount. The numbers in a real return may differ, but the lesson is the same: the depreciation history matters.

That is why a succession plan should not rely on a rough asset list or the farmer's memory. It should be checked against the depreciation schedule and tax records.

Basis oversight can be as costly as a bad sale decision

Income tax basis oversight happens when a family makes decisions without knowing the basis of its assets or how that basis may change at death. The oversight can go in either direction: heirs may assume an asset has a high basis when it does not, or they may fail to document a basis adjustment they are entitled to claim.

Inherited property generally receives a basis determined under federal tax rules, often tied to fair market value at the date of death or an alternate valuation date when properly available. That treatment can differ significantly from a lifetime gift, which may carry over the donor's basis. But the result depends on the facts, the type of property, how it was owned, and how the transfer was structured.

A basis adjustment can reduce taxable gain if heirs later sell property. For depreciated equipment, it may also change the amount of gain subject to recapture on a later sale. But families should not assume that every transfer gets the same treatment or that an estate plan automatically produces a favorable basis result. Trust terms, ownership, prior gifts, elections, and the timing and nature of a sale all deserve review.

This is where generic "a trust fixes everything" advice can cause confusion. A trust can help accomplish legal, management, or distribution goals, but the word "trust" does not answer what basis the beneficiary receives or what income tax follows a sale. Ask the adviser to explain both the transfer mechanics and the expected basis consequences.

Schedule F helps—but it is not a full basis plan

Schedule F reports farm income and expenses on an individual income tax return. It can provide useful information about operating results, but it is not a substitute for a complete asset-by-asset depreciation and basis review. Families need to track property details, including purchase or placed-in-service dates, cost, depreciation claimed, improvements, trade-ins, and any prior dispositions.

When reviewing a farm's records, gather:

- Current depreciation schedules and relevant prior-year tax returns.
- Purchase documents, invoices, titles, and records for major improvements.
- Information about equipment trades, gifts, inheritances, and business transfers.
- Reasonable current values for land, buildings, livestock, and machinery.
- A list of likely sales, buyouts, or changes in use over the next several years.

Resources such as USDA Economic Research Service reports can help families understand broad farm-sector trends and economic conditions. Industry coverage from AGDAILY may also put farm business issues in context. Neither replaces the family's own tax records or advice from a tax professional who has reviewed the specific assets.

Compare the questions each tax system asks

Planning question Estate tax focus Income tax focus What event matters? Transfer at death, under applicable rules Income, sale, exchange, or other taxable transaction What information is central? Ownership and value of assets, deductions, and applicable exclusions Tax basis, depreciation, sale price, and transaction structure Who should be considered? The estate and its beneficiaries The owner, business, and whoever may later sell or receive the asset What can go wrong? A plan overlooks an estate tax obligation or liquidity need A sale or transfer creates taxable gain the family did not anticipate

Build the plan around the likely next transaction

Good planning starts with the family's intended use of each asset. If a successor plans to keep operating the farm and using the equipment, the tax analysis may look different from a situation where the equipment will be sold to fund a sibling buyout. If land will be divided, rented, or sold, that path should be discussed before the documents are signed—not after an heir receives a surprise tax bill.

Ask the farm's attorney, tax preparer, and financial adviser to coordinate on the same practical questions:

1. Who is likely to sell each major asset, and when?
2. What is the current tax basis and depreciation history?
3. Could a sale trigger ordinary income under Section 1245 or another tax rule?
4. Would a different transfer or ownership structure change basis or tax timing?
5. Does the family have cash to pay a tax bill without forcing a rushed sale?

These questions do not produce a one-size-fits-all answer. They do help expose the assumptions that often sit quietly inside an estate plan.

Make tax review part of the annual farm routine

Basis and depreciation records are easier to review before a sale is imminent. Families can schedule a periodic succession checkup alongside tax preparation, then revisit it after a major equipment purchase, land transaction, ownership change, or health event. Keep the asset list, depreciation schedules, and estate documents aligned.

For family members who prefer listening to reading, an audio player such as Instaread may help with general background material about business, finance, or planning concepts. Treat that as a learning aid, not as advice about a particular farm's tax position. The controlling details are in the family's records and applicable tax law.

Protect the farm from the tax bill no one modeled

Estate tax deserves attention when the facts call for it. But for many farm families, the more immediate risk is an income tax bill caused by a sale, a low basis, or depreciation recapture. A plan that focuses only on who inherits the farm may leave out the question that determines whether the heir can afford to keep it.

Review the depreciation schedules. Confirm the basis. Identify who may sell each asset and when. Then make sure the legal plan and tax plan tell the same story. That is how families move from estate tax focused planning toward succession planning that considers what heirs will actually pay—and what they will have left to farm.