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Maintaining Farm Land Homestead Classification and Qualification for Minnesota \$4 Million Qualified Small Business Property Qualified Farm Property Exclusion

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Introduction:

During the 2011 Minnesota legislative session, state lawmakers initiated a Qualified Small Business Property & Qualified Farm Property Exclusion relating to Minnesota estate tax. The \$4 million dollar Minnesota estate tax exclusion for qualified small business and qualified farm property was signed into law July 2011 for decedents dying after June 30, 2011. The exclusion is per qualifying individual and is in addition to the Minnesota \$1 million estate tax exclusion available to every individual in the state.

Legislative law tied qualifying for the farm property exclusion to maintaining homestead classification on farm land until death. If homestead classification is lost before the decedent's death, the estate will not qualify for the additional exclusion. Many folks feel qualifying is not going to be a problem and the exclusion is a panacea for eliminating Minnesota estate tax upon their death. However, without planning and maintaining homestead classification, there could be major issues.

Following is a list of farm land ownership and homestead classification scenarios. Note there are several scenarios where the decedent could lose homestead classification and therefore not qualify for the exclusion. There are many scenarios of ownership and this is only a partial list. Additional homestead classification information can be found in Minnesota Statute 273.124. Check with your county assessor for details specific to your situation.

<u>Scenario</u>	<u>Homestead Qualified</u>	<u>MN \$4 Million Exclusion Qualified</u>
Landowner lives on the land. Landowner farms the land.	Yes (Regular Ag) ¹	Yes
Landowner lives on the land. Landowner cash rents land to an unrelated tenant, crop-shares or custom farms the land.	Yes (Regular Ag) ¹	Yes
Landowner lives in town within 4 contiguous cities/townships or a combination thereof from the land. Landowner is actively engaged in farming the land.	Yes (Active Farming) ²	Yes

Scenario

Homestead Qualified

**MN \$4 Million
Exclusion Qualified**

Landowner lives in town within 4 contiguous cities/townships or a combination thereof from the land. Landowner's qualified family member⁴ lives on the land and farms the land.

Yes (Ag-Relative)³

Yes

Landowner lives in town within 4 contiguous cities/townships or a combination thereof from the land. Landowner's qualified family member⁴ does not live on the land but farms the land.

Yes (Active Farming)²

Yes

Landowner lives in town within 4 contiguous cities/townships or a combination thereof from the land. Landowner's qualified family member⁴ lives on the land but does not farm the land. The land is cash rented to an unrelated non-family tenant.

Yes (Ag-Relative)³

Yes

Landowner lives in town within 4 contiguous cities/townships or a combination thereof from the land. Landowner's qualified family member⁴ does not live on the land and does not farm the land. Landowner cash rents the land to an unrelated non-family tenant.

No

No

Landowner lives in town within 4 contiguous cities/townships or a combination thereof from the land. Landowner's qualified family member⁴ does not live on the land and does not farm the land. Landowner crop-shares the land.

No

No

Scenario

Homestead Qualified

**MN \$4 Million
Exclusion Qualified**

Landowner lives in town within 4 contiguous cities/townships or a combination thereof from the land. Landowner's qualified family member⁴ does not live on the land and does not farm the land. Landowner custom farms the land.

No

No

Landowner lives in town but is not within 4 contiguous cities/townships or a combination thereof from the land.

No

No

Land is in an authorized entity⁵. Landowner is a member of the entity and lives on the land. Landowner is actively engaged in farming the land.

Yes (Active Farming)²

Yes

Land is in an authorized entity⁵. Landowner is a member of the entity and lives in town within 4 contiguous cities/townships or a combination thereof from the land. Landowner is actively engaged in farming the land.

Yes (Active Farming)²

Yes

Land is in an authorized entity⁵. Landowner is member of the entity but does not farm. Landowner a) lives on the land or b) lives in town within 4 contiguous cities/townships or a combination thereof from the land. Landowner cash rents the farm land to a qualified family member⁴ who **is not** a member of the entity.

No

No

Land is in an authorized entity⁵. Landowner is member of the entity but does not farm. Landowner a) lives on the land or b) lives in town within 4 contiguous cities/townships or a combination thereof from the land. Landowner rents the land to a qualified family member⁴ who **is** a member of the entity.

Yes (Active Farming)²

Yes

Scenario

Homestead Qualified

**MN \$4 Million
Exclusion Qualified**

Landowner lives on the farm and the farm land qualified for homestead classification. Landowner has to enter an assisted living, nursing home or other health care facility that is a) within 4 contiguous cities/townships or a combination thereof from the land or b) is not within 4 contiguous cities/townships or a combination thereof from the land⁶.

Yes (Regular Ag)¹

Yes

Landowner lives on the land and farms the land. Landowner goes south each winter but Minnesota is their state of residence⁶.

Yes (Regular Ag)¹

Yes

Landowner lives in town within 4 contiguous cities/townships or a combination thereof from the land and a qualified family member⁴ farms the land. Landowner goes south each winter but Minnesota is their state of residence⁶.

Yes (Active Farming)²

Yes

Land in Trust:⁷

Placing land in trust is a very common estate planning strategy. However, if not done properly this approach can cause challenges to maintaining homestead classification. The type of trust is not the current concern regarding homestead classification. Property can be placed in a testamentary, *inter vivos*, revocable, or irrevocable trust but regardless of type, the trust does not receive the homestead classification. For homestead purposes, trusts are considered entities, not individuals. It is the grantor (person establishing the trust) or individuals of specific relation to the grantor that may be eligible for homestead. The grantor of the trust is considered the owner for homestead classification purposes. Homestead is granted in the name of the qualifying occupant – trust grantor, grantor’s surviving spouse, or qualified relative occupying the property. The individual also needs to be a Minnesota resident to qualify. In addition, these same rules apply to life estates and transfer upon death deeds.

Owner-Occupied, Trust Held Homesteads:

Land held in a trust is eligible for homestead classification **if** the grantor or grantor’s surviving spouse of the trust occupies and uses the property as a homestead. If the grantor passes away and the trust is not dissolved, the grantor’s surviving spouse can occupy the property and it will continue to receive homestead classification. If the trust is dissolved, homestead classification will be based upon ownership and occupancy facts after the trust is dissolved.

Relative Trust-Held Homesteads:

Property held in trust can receive relative homestead if it is occupied by a qualified relative of the grantor of the trust. The relative or surviving relative of the grantor must occupy and utilize the property as a homestead to qualify for homestead classification.

For agricultural property held in trust, a qualified relative includes a child, grandchild, sibling or parent of the grantor of the trust. Any of these individuals must be a Minnesota resident to qualify for the homestead classification.

Linking Trust-Held Properties:

Property owned by different entities (trusts for example) **cannot** be linked or considered part of the same farm for homestead classification purposes. All property held in trust must have the same owner/ownership to qualify for homestead.

Here is an example of a married couple, each who have land in their respective trusts. Mr. A has a trust with land in it. He has homestead on the house, garage and one acre of land plus the additional farm land in his trust. Mrs. A has her own trust with additional and separate farm land as part of her trust. Since Mr. A already has the homestead classification, Mrs. A cannot link her land with Mr. A's land and get homestead classification on her acres as well. Only one individual in this case can receive homestead classification. If Mr. and Mrs. A were grantors of the same trust with all their land in that trust, they would be considered joint owners of the trust and therefore all the land would be eligible for homestead classification. This also applies to an individual who owns land that is part of a partnership and owns additional land that is part of a corporation. These acres cannot be linked for homestead classification on all the acres collectively.

There are three exceptions to these rules as follows:

- 1) The homestead of a base parcel owned and occupied by an individual may be linked to a parcel of property that the owner owns with other individuals;
- 2) The homestead of a base parcel owned and occupied by an individual may be linked to a parcel of property that is owned by a trust and the individual owners of the parcel are the grantors of the trust-held property (and vice versa); and
- 3) In the case of married couples, properties that are held solely in the name of one spouse may be linked to parcels that are held solely by the other spouse and parcels that are titled in both names. This does not apply to any entities of which the husband and/or wife are both members. It only applies to parcels owned by natural people.⁷

If you change ownership of property from sole ownership to placing that property into a trust, you will lose homestead classification. However, homestead classification can be reinstated by simply completing the "Application for Homestead Classification for Property Held Under a Trust" and returning the form to your county assessor by December 15th. This is also the case for any "Special Agricultural (Actively Farming) Homestead" which includes land leased to an authorized entity, land owned by an authorized entity, property held in trust and leased to an authorized entity and land owned by an authorized entity and occupied by a qualified person. An authorized entity includes a family farm corporation, joint family farm venture, family farm limited liability company and a partnership which is operating the family farm.

As you can see, depending upon how land is held and owned, homestead classification can be a complex issue. Homestead classification is only one of many issues that need to be addressed when developing and implementing a farm business transition and associated personal estate plan. One small omission or incorrect selection can be costly. For clarification on homestead classification, it is best to visit with your county assessor for information specific to your situation. In addition, seek qualified professional legal help when engaged in the farm transition and estate planning, development and implementation process.

Footnotes:

¹ Regular Agricultural Homestead is a single, one-time application requirement until law changes. See MS.273.124, subd. 1(a).

² Active Farming Homestead is an annual application requirement. See MS.273.124, subd. 14(b), clause (i).

³ Agricultural Relative Homestead is a single, one-time application requirement until law changes. See MS.273.124, subd. 1(d).

⁴ Qualified family member includes landowner's spouse, landowner's or landowner's spouse's son, daughter, grandson, granddaughter, siblings, and parents.

⁵ An "Authorized Entity" includes such things as a family farm corporation, joint family farm venture, family farm limited liability company, or a partnership which is operating a family farm. For information specific to your situation, see your county assessor.

⁶ When entering a health care facility or traveling out of state for the winter, you can retain homestead classification. This is referred to under state law as a "temporary absence". If traveling out of state, Minnesota has to be your state of residence to maintain the homestead classification in Minnesota.

⁷ Information source: Minnesota Department of Revenue Bulletin, "Trust properties and homestead determination", Information & Education Section, Property Tax Division, www.revenue.state.mn.us.

