

# Ag Succession

Succession Planning in Agriculture

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## ***Enduring Powers of Attorney in Farm Operations***

*The purpose of the Ag-Succession series of factsheets is to provide an objective overview of the issues and options related to succession planning. This information should not be a substitute for using a lawyer, accountant or financial planner to help you make a thorough assessment of your specific operation and situation.*

### **An Essential Planning Tool**

An enduring power of attorney is an essential estate planning tool for all farmers. It is as important as a will.

A power of attorney is a document that appoints a person, called the attorney, to manage a person's property.

For example, if mother and father are leaving on an extended holiday, they can sign a power of attorney that appoints the farming child as the attorney to negotiate and sign a surface lease with an oil company. This type of power of attorney can be restricted for only the purpose of negotiating the surface lease with one quarter section of land. It can also be a very general power of attorney that gives full authority to the farming child to make all decisions about all assets, including bank accounts. Upon return from their holidays, the parents can revoke the power of attorney.

An ordinary power of attorney is revoked automatically if the person who signs it, called the donor, becomes incapacitated. An enduring power of attorney endures or continues if the donor becomes incapacitated. All powers of attorney are revoked on death. At that point the will comes into effect.

### **Types of Enduring Powers of Attorney**

There are two types of enduring powers of attorney: a continuing or immediate power, and a springing power.

A continuing enduring power of attorney is effective as soon as it is signed and continues (endures) if the donor becomes incapacitated. This type of power is usually used for someone who is elderly and no longer wishes to be bothered with day-to-day decisions, such as paying bills. It can also be useful in the example above where the farming parents are on a winter holiday. However, a better solution might be to use an ordinary power of attorney for that specific purpose, backed up by a more general, springing enduring power of attorney to be used in the event of incapacity.

A springing enduring power of attorney is only effective in the event of incapacity. It springs into effect when the donor becomes incapacitated. Other contingencies that spring the document into effect can also be specified. The document should name a person who decides when the contingency has occurred. Most people state that a doctor decides when the donor is no longer capable of managing his or her own estate. When the doctor signs a declaration to that effect, the power of attorney springs into effect. The donor can name others to make the decision. Other options include a spouse or



perhaps a majority vote by the children. If no one is specified to make the decision, then two medical doctors must decide whether the power of attorney springs into effect.

## Choice of Attorney

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Choosing an attorney is as important as choosing an executor, but the role of the attorney is quite different from that of an executor. An executor distributes the estate to the beneficiaries after death. An attorney must preserve property for the benefit of the donor for the remainder the donor's life. The attorney must therefore be trustworthy and have good business sense. It is useful if the attorney resides near the donor, but this is not absolutely necessary.

Many people choose their spouse as the attorney and one or more of the children as alternate attorneys. If one parent becomes incapacitated, the spouse can act as attorney, but if the spouse later becomes incapable or dies, the alternate attorneys take over.

Sometimes it may be appropriate to choose the farming child as the attorney. If the parents have started their succession plan by transferring some of the farming assets to the farming child, that child might be most interested in managing the estate. However, the farming child may be in a conflict of interest by acting as the attorney, as well as carrying on the farming business. Parents might want to consider appointing one or more of the non-farming children as attorneys, perhaps together with the farming child. This is particularly important when the parents' non-farming assets need to be preserved for their retirement and eventual distribution to the non-farming children through their wills.

Particularly in farming operations, there is a fine balance between protecting the long-term security of the parents against the goal of carrying on the family farm operation as a viable economic unit. If a farming child is one of the attorneys, he or she may be in a conflict of interest if allowed to make decisions concerning the farming operation, as they may unduly benefit the attorney (such as purchasing farm assets). It is therefore important that this conflict be removed or balanced by the addition of another of the children or perhaps somebody totally independent who can make decisions when the farming child is in a conflict of interest. If the farming child is named as the sole attorney, then additional powers need to be added to the power of attorney to deal with this conflict of interest.

## Powers of the Attorney

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An attorney has the power to do anything that the donor may lawfully do by an attorney. This means that the attorney may sell land, change investments, pays the donor's bills, etc. An attorney may not however, make a will for the donor. Only the donor can do that, and only when capable.

The property of the donor can be used only for the donor, and the maintenance, education, benefit and advancement of the donor's spouse, adult interdependent partner and dependent children. If the children are independent adults, they may not use any part of the estate for themselves, unless the power of attorney allows for this. Additional powers are therefore needed if the donor wishes to allow the farming child to benefit from the farming operation.

An attorney cannot make a profit from the donor's assets unless specifically allowed by the document. This could mean that the farming child is required to rent the parents' farmland at fair market value in the event of incapacity of the parents. If it is intended that the farming child continue the business, then the attorneys should be given power to enable this. If the farming child has been sharing the farm income with the parents, such as taking a percentage of partnership income, then this should be addressed in the power of attorney. In other words, the parents need to change the general rules if they want the farming child to benefit from their property in the event of incapacity. But this should be balanced with security for the parents in their old age and preserving assets for their estate for eventual distribution to all their children through their will.

Each enduring power of attorney has to be specifically designed to meet the needs of each family farm, and updated as the farm estate plan evolves. A 35-year-old couple with minor children might have a very general enduring power of attorney allowing for the maintenance of their young children. A farming couple with children in their late teens or early twenties, who are just beginning to get involved with the farming operation, may need a power of attorney with a lot of flexibility to allow their attorneys to use their discretion with respect to the children's involvement in the farming business. As the children grow older and the farming children acquire an interest in some of the farming assets, the donor may wish to allow for the children to purchase the farming operation, perhaps at less than market value, in order to allow for the continuity of a viable farming operation.

Since the property may only be used for the benefit of the donor, the attorney may not make any gifts to anyone, unless this power is given in the enduring power of attorney. This could be as simple as allowing the attorneys to make gifts to grandchildren on special occasions. It might also give the power to gift some farm assets to the farming child or allow for a sale at less than fair market value. This type of power should be included with caution as it is important to preserve the estate of the parents for their retirement. The attorney would also be in a conflict of interest if the attorney is the farming child. Additional safeguards should be included such as the appointment of independent attorneys or the approval of the gifts by independent parties.

Attorneys are prohibited from purchasing any assets of the estate that they administer, unless the power of attorney specifically allows. The Land Titles Office will not allow the attorney to transfer land to the attorney unless the power of attorney specifically allows for this.

## The Impact of the Prudent Investor Rule on Farm Enduring Powers of Attorney

Before February 1, 2002, attorneys had no restrictions on the investment of assets they were administering under a power of attorney. An attorney is not a trustee and was therefore not subject to the restricted investments under the *Trustee Act*. An attorney, of course, had to be careful to ensure that the assets were properly invested, but there was no restriction on the types of assets that could be retained.

Effective February 1, 2002, the *Trustee Act* was amended in ways that have a major affect on farm enduring powers of attorney:

- The new Act adopts the prudent investor rule.
- The prudent investor rule applies to all attorneys exercising a power of investment under an enduring power of attorney, no matter when it was signed, unless the power of attorney provides otherwise.
- If the enduring power of attorney specifically adopted the powers of investment under the *Trustee Act*, then the attorney is restricted to the types of investments known as the “legal list.” This is a major problem because land is not an authorized trustee investment.

The *Trustee Act* is subject to a contrary intention. A farm enduring power of attorney should therefore change the rules by allowing for the retention of the farm assets. If it is intended that the farm be retained, the power of attorney should not adopt the old *Trustee Act* nor the schedule under the new *Trustee Act* because this would adopt the old legal list approach under which land is not an authorized investment.

The prudent investor rule is a good development in the law of trusts. The essence of the prudent investor rule is, “Don’t put all your all your eggs in one basket.” Diversification is the key. Modern portfolio theory provides that investment risk may be managed through the use of a properly diversified portfolio, such as would be maintained by a reasonably prudent investor. The goal of the prudent investor is not simply to minimize risk to the investments held on behalf of the trust, but to choose a portfolio that achieves an optimal relationship between expected return and risk.

The problem with the prudent investor rule is that farmers tend to put all their eggs in one basket. The vast majority of a farmer’s estate is usually invested in the farm business. Farmers are perfectly entitled to put all their eggs in one basket while they are alive and capable. But in the event of incapacity, the attorney is subject to the prudent investor rule and might therefore be required to diversify the investments. This may lead to a sale of the farm. If this is not what is desired, then the power of attorney should specifically allow for the retention of the farm assets and allow for carrying on the farming business.

If the power of attorney does not have these types of powers, there is an argument that can be used to allow the farm assets to be retained. The *Trustee Act* provides that trustees and attorneys must take certain criteria into account in planning the investments of the trust.

One of these factors is “the special relationship or value of an asset to the purposes of the trust or to one or more of the beneficiaries.” It is therefore arguable that the intention of the parents was to preserve the family farm and that it eventually pass it to the next generation. It can also be argued that the farm has a “special relationship” to the parents and eventually the farming children. Therefore, it should be retained.

If there is any discord in the family, such as non-farming children arguing that the farm should be sold, it is preferable to have these issues dealt with specifically in the enduring power of attorney.

## Signing Requirements

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An enduring power of attorney must be signed before a witness. The witness cannot be the spouse of the donor, the attorney or the spouse of the attorney. Effective June 1, 2003, an enduring power of attorney may not be witnessed by the adult interdependent partner of the donor, the attorney nor the adult interdependent partner of the attorney.

## Conclusion

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An enduring power of attorney is an essential part of every estate plan and it is particularly important in a farm estate plan. There are some very special issues to be considered in preparing an enduring power of attorney if it is intended that the farm be preserved so that it can pass to the next generation.

## Glossary

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**Donor:** The person who signs the power of attorney.

**Attorney:** The person (or trust company) who is appointed to manage the property under the power of attorney. An attorney should not be confused with a lawyer.

**Power of Attorney:** A document that appoints an attorney to manage a person's property. An ordinary power of attorney is revoked if the donor becomes incapable.

**Enduring Power of Attorney:** A power of attorney that continues (endures) if the person becomes incapable or comes into effect if the person becomes incapable.

**Continuing Enduring Power of Attorney:** An enduring power of attorney that continues (endures) if the person becomes incapable. This is also called an immediate enduring power of attorney.

**Springing Enduring Power of Attorney:** An enduring power of attorney that comes into effect (springs into effect) if the person becomes incapable. One might also provide other contingencies that spring the power of attorney into effect.

**Powers:** The things that an attorney can do with the donor's property (e.g., sell, lease, purchase, invest, pay bills, collect money, etc.)

**Capacity/Capable:** The ability to understand how to manage one's property; to make reasonable judgments about one's property. A person must be capable in order to sign an enduring power of attorney, or else it is not valid.

**Adult Interdependent Partner:** This is a common-law spouse, including a same sex partner, now defined under the *Adult Interdependent Relationships Act* that went into effect June 1, 2003. A person is the adult interdependent partner of another person if the person has lived with the other person in a relationship of interdependence for a continuous period of not less than three years, or if there is some permanence and a child of the relationship by birth or adoption. Another example is if a person has entered into an adult interdependent partner agreement with the other person. A family member may not become an adult interdependent partner of a person unless they sign an adult interdependent partner agreement.

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### For More Information

Alberta Agriculture, Food and Rural Development's website: <http://www.agric.gov.ab.ca>

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