

Farm Succession Planning

Presented by

Ron Dvergsten; FBM Instructor and

Jeff Reese; CPA, EA

Farm Succession Planning

Key Question

Do you want your business to
continue beyond your lifetime?

Reasons people avoid succession planning

- Raises unpleasant family issues
- Forces people to confront their mortality
- Inability to choose among children or make decisions on distribution of assets
- Too busy doing day-to-day tasks
- Loss of control
- Loss of identity
- Too dependent on the assets for their later years' expenses
- Reduces options
- They don't know how to plan

FARM

Business

Assets

Financial
Viability

Goals

Succession
Plan

Retirement
Plan

Estate
Plan

Estate
Plan



Long Term Financial and Management Viability

- Access & control of essential business assets- by the primary operator
- Adequate size for feasible business
- Debt structure
- Feasible cash flow
- 3-M's
 - Money
 - Management
 - Marketing

Prerequisites for the Desired Outcome in Succession Planning

- All involved must possess a **genuine desire** for the farm business to continue for another generation. (Note: we did not say next generation)
- All involved must possess an openness to objectively evaluate all perspectives/opinions- **including their own.**
- All involved must understand that they may not be able to respect all conflicting perspectives/opinions equally in the planning process.
- All involved must act with openness and objectivity and must genuinely commit to perform the required actions to carry out the plan

Business Resource Inventory and Analysis

- Physical Assets- Short-term (crop, feed, market livestock), intermediate, (Machinery and breeding livestock) and long-term (land and Buildings) property
- Financial- Income Statements, Balance Sheet, financial measures, Trend information, and cash flow
- Personnel- Human asset inventory (Who may be impacted by the plan)

Another Key Concept

Family Businesses need to separate/distinguish **family time** from **work time**

Grandpa's idea of family time may have been "baling hay" or "working cows"; that most likely would not meet family time expectations of today.

Now- It maybe something like. What do you mean you want we to work every other weekend or "I may occasionally need to work 60 plus hours in a week."

How we define "family": the priorities, expectations, relationships, and measures of success in a family are, and should be, different than those used to measure success in a business.

Attributes of a Successful Family vs a Successful Business

Successful Family

- Loving
- Loyal
- Affectionate
- Supportive
- Empathetic
- Understanding
- Enduring
- Communicative

Successful business

- Efficient
- Profitable
- Goal Directed
- Effective
- Aggressive
- Evaluative
- Innovative
- Proficient

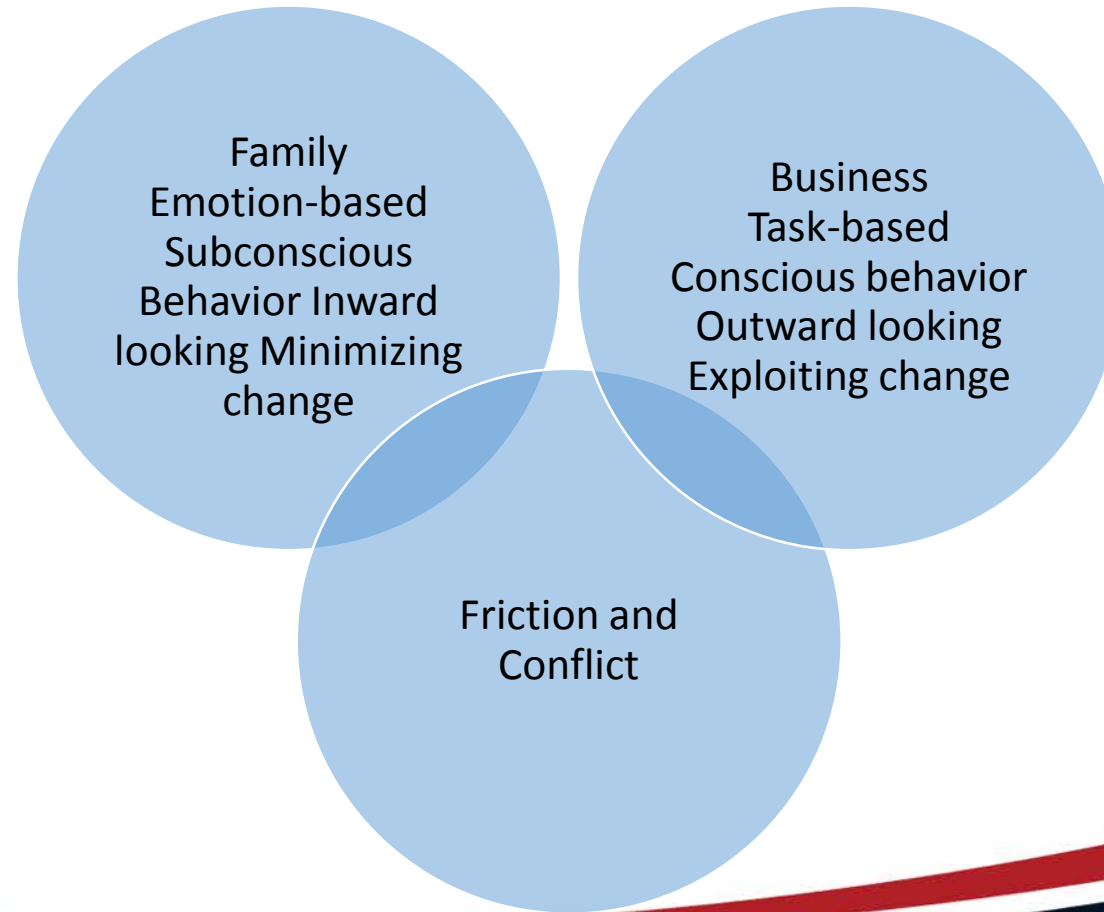
Identifying the System

- It is imperative that families identify the system that is appropriate for the situation.

It is appropriate to behave as a family at a holiday gathering.

It is not appropriate to behave as a family at a business meeting.

Clash Of The “Systems”



Farm Succession Planning in a Nutshell

- Treat farming as a business.
- Develop a succession plan.
- Identify values.
- Create a vision.
- Define the mission.
- Establish personal and business goals.
- Determine the objectives.
- Carry out the strategies.

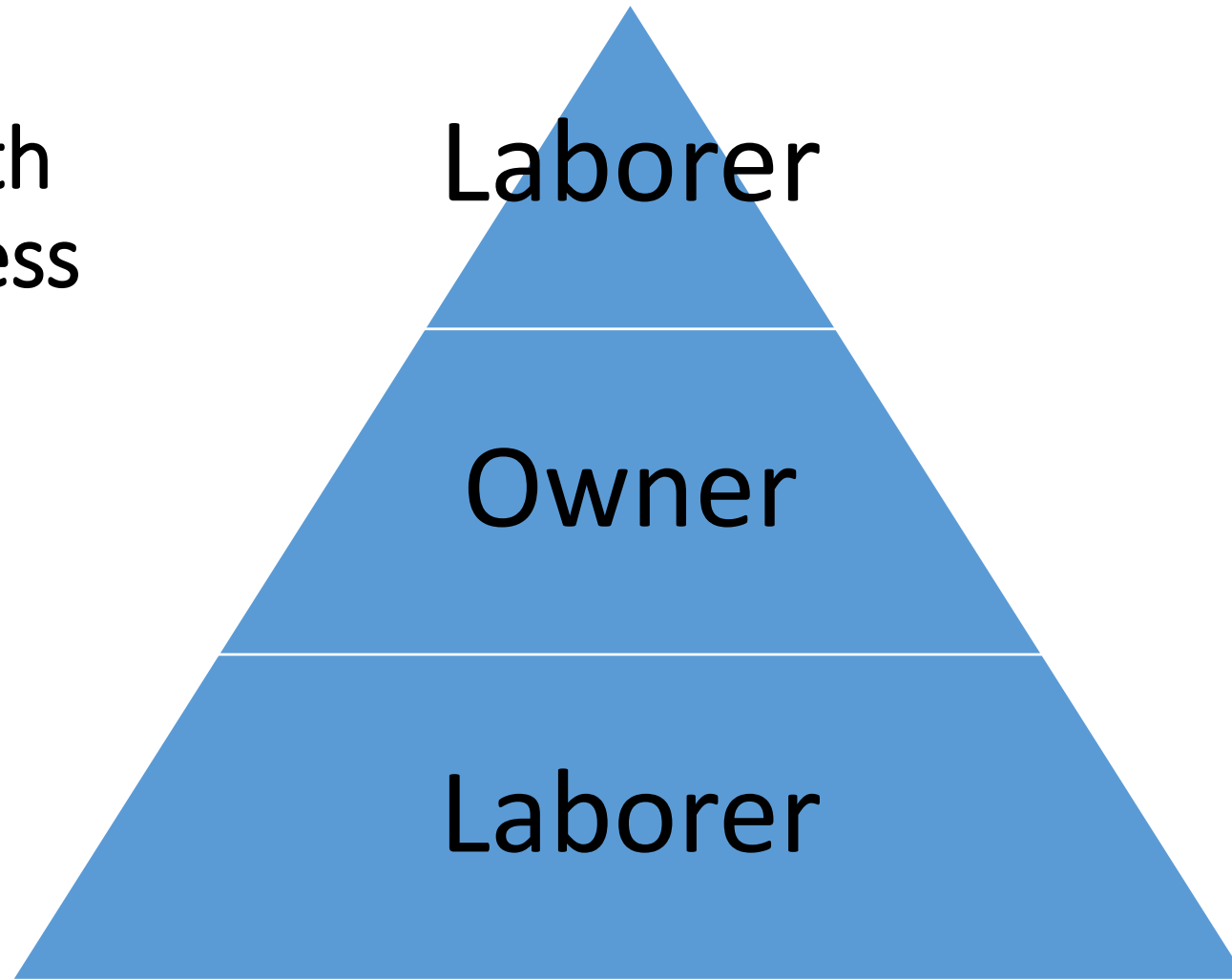
Farm Succession Planning in a Nutshell (con't)

- Practice effective communication.
- Learn and use a business vocabulary.
- Identify for yourself and others the role you are assuming.
- Develop written job descriptions for all roles in the farm family business.
- Use the skills to mutually resolve conflicts.
- Trust the process of planning.
- The business must have long term financial viability.

GOLDEN RULE!!

The person with the
Gold (Assets) gets to
make the rules!

Common Growth Cycle of a Business



How long will your transition/transfer period last?

- Most successful farm transitions will take 7-10 years to execute
- Defined goals
- Circumstances
 - Age
 - Health
- Finances
- Desires
- Abilities

6 Basic Questions for Estate Planning within the farm transition process

- What do I own?
- How do I own it?
- What is it worth?
- Who do you want to have it?
- When do you want them to get it?
- How do you want them to own it?

Sometimes the most unfair thing you can do is to treat all your heirs equally

Perceived Tax Liabilities Many Times becomes the Biggest Hurdle to Transition Planning

- Farm transfers are inherently complex
 - Transition planning involves:
 - Economic
 - Legal
 - Tax issues
 - Social/family relationships

Farm Asset Types and Their Tax Attributes

- Raised Breeding Livestock- If held for 24 months- when sold they qualify for long-term capital gains treatment
- Purchased Breeding Livestock- if sold for more than remaining tax basis, income is treated as ordinary income, but not subject to SE tax
- Market Livestock and Crop Sales- Schedule F assets, subject to SE Tax
- Growing Crops- if sold in field with the land, they receive capital gains treatment, and could be spread out if sold on a Contract for Deed
- Land and Beet Stock- capital gains assets
- Machinery and Equipment- can be the “time bomb” in farm transitions if not handled properly

Principles of Transferring the Farm with the Least Tax Consequences

- Gradual is always best
- Allocation can be a major tax saver- page 3 of hand out example
- Gifting can be a selective tool that works to the benefit of both parties: 2017 Gifting rules:
 - \$14,000 annual exclusion per individual (\$15,000 for 2018)
 - \$5.49 million total gift and estate life time limit per individual (tax reform could drastically change this)
 - \$10.98 million for a married couple

Assets gifts: the donor's tax basis becomes the recipient's tax basis

Principles of Transferring the Farm with the Least Tax Consequences : Continued

- Chattel property may be the best place to start
- Always maximize capital gains
- Specify the assets to be bought in a chattel installment sale
- Don't overlook like-kind exchanges
- Don't overlook entities as transfer vehicles
 - LLC's seem to be the preferred entity type at the present time
 - LLC's can easily converted to a corporation

You cannot guarantee Success of Farm Transfers but you can ensure Failure!

- Failure to communicate.
- Failure to treat the farm as a business.
- Failure to develop a succession plan.
- Failure of the owner to retire.
- Failure of the owner to transfer managerial authority, responsibility and accountability.
- Failure to provide adequate compensation to the business successor.
- Failure to develop an equitable estate plan.
- Failure to fully implement the plan.

Succession Planning...
Average Age of MN farmer is 65 years

Don't retire FROM something....

Retire TO something!