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Planning farm succession: how to be successful

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Abstract. Planning farm succession is really good farm planning in its broadest aspect. Unfortunately very few farmers and their families have devoted sufficient time to working out how the farm business will be transferred. After demonstrating the importance of the farm succession issue, this article goes on to explaining a method of successfully tackling the process.

Keywords: succession, transfer, next generation, continuity, business plan.

Introduction

In a business sense, succession planning refers to the orderly transfer of management, responsibility, ownership and control, over time. In a farm business this could mean transferring the ownership of some of the machinery and/or livestock, transferring the management of part of the farm and eventually transferring ownership of the land.

Succession in the business and progression of the individuals' careers are intertwined. Too often when the existing generation decides to move on, nobody is ready and waiting to follow. The next generation has left because of a variety of factors including being chased away or simply a sense of frustration. Alternatively, the next generation is ready to take over before the older generation is ready, or the next generation wants more time before returning to the family business.

Many people leave the family farm because of inappropriate employment relationships, unclear areas of responsibility and a reward package which is well below the industry standard for a non-family employee.

In order to provide sensible advice and guidance it is necessary for the farm management consultant to understand first, why this farmer is farming; second, why he or she is farming this farm; and third, why they are farming this farm in this way. In other words, it is necessary to establish whether or not there are historic constraints which restrict the choices of the farming family in the way they think about the farm as an asset, and whether they see it as a business where they are in control or a business which controls them.

Any succession plan has more chance of working if the people involved start to think about it earlier rather than later. For instance, building some off-farm assets is useful from a risk management point of view and can also make succession planning easier. Farm succession has become an important issue that the Australian farming community needs to deal with diligently and urgently to reduce future shock. This paper attempts to identify some key issues concerning farm succession and share

opinions, formed through many years of practice and observation, about successful farm succession.

The farm succession issue is not new but the significance is increasing

Traditionally farm succession was not a big issue (for the purpose of this paper, the words "farm" and "station", including pastoral leases, are interchangeable). If the eldest son wanted to farm he was given the farm and younger children got what was left over. In cases where the eldest son wanted to pursue another career, a younger son was given the farm. Many farms were big enough to be cut in half and in some cases they were mortgaged to allow the purchase of another farm.

The significance of the issue is increasing because as land prices have increased, the cost-price squeeze has impacted on profitability and a series of dry seasons have combined to make farming unattractive as a career. The result is that in many cases there is no obvious successor. Farm children have been encouraged to pursue other careers.

The issue is causing concern in all parts of rural Australia, but the problem is more acute in areas where there is a long distance to travel to major centres. It is possible that many men who choose to work in remote areas will not be able to attract a life partner to join them. The issue is not confined to any socio-economic group.

How to successfully plan farm succession

To handle farm succession successfully, there are a number of principles to observe. There are also some steps that can be followed and models that can be made use of. In addition, in view of the changing business environment in which farms are operating, new thinking is also encouraged to provide new solutions. These important issues are discussed in this section.

Fundamentals to successful farm succession

When dealing with any farm succession matters, the following important principles need to be observed by those who are involved in succession plan:

- To work out what the existing generation wants to do – where they will live and what they will do in retirement (if succession is an option).
- To identify the needs, aspirations and expectations of each family member in each generation. Sometimes expectations need to be managed.
- To build, maintain and if necessary repair relationships between family members.
- To manage expectations amongst family members.
- To look at transferring management and control of the farm over time.
- To sort out how to transfer ownership of the farm (if that is what you want to do).
- To decide what deal there should be for the incoming generation and what provision to make for the non-farming children.

Traditionally, succession planning advice has been the province of accountants, lawyers or financial planners. But other advisors who can assist with 'people' and farming issues may also need to be part of the planning process using a team approach. The team of advisors needs to agree with the client on a pathway to:

- Establish the parents' (or whoever holds the 'keys') broad direction;
- Understand the desired direction of all family members; and
- Collect information and to develop a plan. The plan may involve looking at the productivity and profitability of the farm. The collection of information is sometimes complex and includes:
 - Land ownership – which individuals or entities are the registered owners?
 - Livestock – which individuals or entities are the owners?
 - Machinery – which individuals or entities are the registered owners?
 - What is the financial situation and how is the business performing?
 - Are there any non-farm or underperforming assets (beach house, lifestyle block)?
 - What is the debt/equity ratio?

A farm succession plan may take years to develop and decades to evolve. Much time may be spent considering legal structures. Many people get confused about the use of different legal structures such as trust, partnership, company or sole trader, or their combinations. Once the size of the task is understood then the structures and the number and nature of entities required should be reasonably easy to identify. It must

be noted, however, no changes should be made to ownership or structure without accounting, taxation and legal advice.

In preparation for developing a farm succession plan, some essential facts and figures need to be collected which include:

- Who owns what – land, plant, stock
- Assets and liabilities
- Unofficial loans and book loans within family
- Issues of un-paid or under paid wages to family members.

To ensure the drawing up of a good farm succession plan, the following steps should be followed:

- First, ensure that all the advisors are all working for the family as a whole.
- Second, the key family members should meet with the project manager to work out who and when should attend further meetings. Give an outline of the process. Think about in-laws – in or out.
- Third, get the key people committed from each generation – set the ground rules: play the ball not the person and if you are driving the plan do not take sides.
- Finally, it can also be very useful to draw up a genogram as demonstrated in Figure 1. In a genogram, there can be scores of relationships, and attention may need to be given to all of them.

New thinking for better solutions

The issues of farm succession will not be fixed by the same thinking which has brought us to the present situation. New thinking will accept that landowners do not have to farm it and farmers do not have to own land. The ownership of land, water, livestock, machinery and equipment can be separated. Labour can be provided on a contract basis.

Currently succession occurs when the older generation has had enough or when the younger generation pushes to make it happen. New thinking will allow a bridging period where the older generation can slow down while the business keeps expanding, but the next generation family member is not ready to take over. In these situations some arrangement with an employed manager, share farmer or equity partner can assist in the transition.

Where families start to address succession issues earlier in life they can start to provide for non-farming children with off-farm investments. If parents want to provide for non-farming children a smaller share sooner may be an acceptable outcome. The principle of net present value (less money can be provided now, rather than at some future date and be of equal value) is a useful tool.

The most important factor is to get the issues on the table so they can be discussed by the family as a whole.

Some new tools can also be used to aid farm succession planning. One of them is the Farm Succession Planning Score Card developed by Mike Stephens and Associates in 2005 as shown in Table 1. This score card can be used by any families who have a family member who is going to commence work in the family farm business.

It is important to ensure that all participants in the business, family and non-family, individually, fill in the first two sections of the score card. And that all family members fill in the whole card. If it is only filled in by a few members of the team it is unlikely that the result will be a true reading of the situation. Once all members of the team have completed the card, there should be honest and open discussion about why people have recorded the scores in the way they did. As with any benchmarking, the story behind and the reasons for the number are often more important than the number itself.

The scores themselves are not a "Pass/Fail" situation. For example, a 50% score on the whole card with all the points scored in the first two sections indicates that there has been no investment in succession. There is no statistical rigour to the numbers. The card is a simple tool to promote discussion and point to best practice.

A case study

Kirsty McNabb has recently returned home after successfully studying Agricultural Science and completing her bachelor degree.

She agreed to come home because her father (Harry) and mother (Sally) had been running the farm, understaffed, and had a job vacancy. The ownership of the farm is complicated because Harry's father (Ted) still owns most of the land and is keeping his succession plans to himself.

The farm has a mixture of sheep, cattle and crops and Harry is the manager, Sally manages the books and the cattle, and Ted, although supposedly retired, spends most of most days on the farm.

When, at the completion of her last academic year, and immediately before harvest, Kirsty agreed to come home she agreed that they could sort the details out later. When, four months later, nothing has happened, Kirsty searched the web, found the score card and printed five copies.

Kirsty's next step was to give a copy of the score card to her mother, father, and grandfather and keep two for herself. She secured agreement from each family member that they would fill in the scorecard and

return it to her. Kirsty filled in one herself. She also secured agreement (reluctantly) from her grandfather that they would meet to discuss the completed cards and fill in the last one when they had reached agreement on areas where individuals had differed.

The value of the scorecard was highlighted in the discussion.

Sally had started a job description for Kirsty, but Harry disagreed with some aspects of the job as described. Sally had also completed a job description for herself and there was agreement that it covered her situation, but there were no job descriptions for Harry and Ted. There was no organisational chart and Kirsty pointed out that at times she was unsure whether she was reporting to Sally, Harry or Ted and that she found it confusing. They agreed that a chart which clearly showed who was responsible for each area of activity, and reporting lines, would be useful. Sally had letters of appointment for all but one contractor and resolved to attend to that situation.

The family agreed that unless all jobs are properly described, areas can be neglected or people can start to trip over each other. They also agreed (although Ted grizzled) that they needed an organisational chart.

The family did not do so well with the second section of the scorecard.

There was no induction process. Salary and payment details had not been agreed or documented. Other benefits, including holidays and days off, were vague.

Kirsty pointed out that although she had grown up on the property, she had been away at school and university and there needed to be an agreed procedure in the event of an emergency. She needed to understand the OH&S policies and procedures, and without being demanding about the level of pay and the other conditions she needed to understand what they were.

Filling in the card gave the family the opportunity to discuss the issues of pay, conditions, induction, OH&S and related issues in an environment of cooperation. Tasks to address the deficiencies were allocated to Sally and Kirsty.

The Succession Planning section of the scorecard yielded a mixed response.

Kirsty, her younger brother, and her parents (Harry and Sally) have a really good understanding and open and honest communication about the subject. Kirsty knows that both Harry and Sally want to see the farm remain in the family and that her younger brother may also want to farm. The

future ownership aspirations and expectations have been managed well. The difficulty in this section is that Ted still does not say exactly what he intends to do.

The process has put further pressure on Ted to start to show his hand. The process has highlighted the need to address this area and try to get Ted to tell people what he wants to see happen.

When they got to the last section they agreed that the score should be a C (“Some discussion, but no documentation”).

Concluding comments

Succession planning is a process, not an event. It is a process which should emphasise the needs of the people and the business. When it is clear what those needs are, the accounting and legal issues can be addressed. Succession planning requires a team approach.

Many families put off succession planning because of external factors such as poor seasons or prices. No business is immune from these external factors. However, the planning process should not be postponed indefinitely because of external factors. Once a plan is in place, the family can wait. When the season or prices are in their favour, the plan can be implemented.

More often it is internal, family issues which inhibit progress. In most families delay causes frustration, which in turn, leads to disharmony or real infighting. Plans which are developed and understood, by the whole family, while the guiding hand of the older generation is present, have a greater chance of success.

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Appendix

Table 1. Succession Planning

SCORE CARD FOR FAMILY FARM BUSINESS	
(To be filled in separately by each family member)	
<p>Job Description (Are jobs adequately described and documented?)</p> <p>Is there an organisational chart Tick</p> <p>A position description for <input type="checkbox"/></p> <ul style="list-style-type: none"> ▪ returning family member <input type="checkbox"/> ▪ family members currently on property <input type="checkbox"/> ▪ other permanent staff <input type="checkbox"/> ▪ casual employees <input type="checkbox"/> <p>A letter of agreement for all contractors <input type="checkbox"/></p>	<p>Number of ticks x 5 = <u> </u> / 30</p>
<p>Conditions of employment for all employees including family members Tick</p> <p>Is the induction process documented? <input type="checkbox"/></p> <p>Is the induction process followed? <input type="checkbox"/></p> <p>Are salary and payment details agreed and documented? <input type="checkbox"/></p> <p>Are other benefits agreed? (e.g.: Housing, Meals, Vehicle, Fuel, etc) <input type="checkbox"/></p> <p>Is time off agreed? <input type="checkbox"/></p> <p>Number of holidays days agreed? <input type="checkbox"/></p>	<p>Number of ticks x 5 = <u> </u> / 30</p>
<p>Succession planning Tick</p> <p>Have the expectations of each family member been managed <input type="checkbox"/></p> <p>Are the needs and aspirations of each person in each generation understood? <input type="checkbox"/></p> <p>Is the parents' broad direction agreed? <input type="checkbox"/></p> <p>If the farm is to be passed on, is equity and profitability transparent? <input type="checkbox"/></p>	<p>Number of ticks x 5 = <u> </u> / 20</p>
<p>Succession Plans – Answer either A or B or C or D Tick</p> <p>Full plan documented and agreed <input type="checkbox"/> 10</p> <p>A All family members have been included in discussions <input type="checkbox"/> 5</p> <p> All family members have been informed <i>“Excellent”</i> <input type="checkbox"/> 5</p> <hr/> <p>B Discussions commenced and progress documented and available <input type="checkbox"/> 10</p> <p> <i>“Excellent! Let’s keep the ball rolling”</i></p> <hr/> <p>C Some discussion, no documentation <input type="checkbox"/> 5</p> <p> <i>“Well done! A great start, lets ensure that documentation occurs”</i></p> <hr/> <p>D No discussion between generations <input type="checkbox"/> 0</p>	<p>Total = <u> </u> / 20</p>
<p>Total all sections</p> <p> Job description <u> </u> (30)</p> <p> Conditions of employment <u> </u> (30)</p> <p> Succession Planning <u> </u> (20)</p> <p> Succession Plans <u> </u> (20)</p> <hr style="width: 50%; margin-left: auto; margin-right: 0;"/>	
<p>© Mike Stephens and Associates 2005 Grand Total <u> </u> (100)</p>	

Figure 1. Genogram that can be used in farm succession planning

