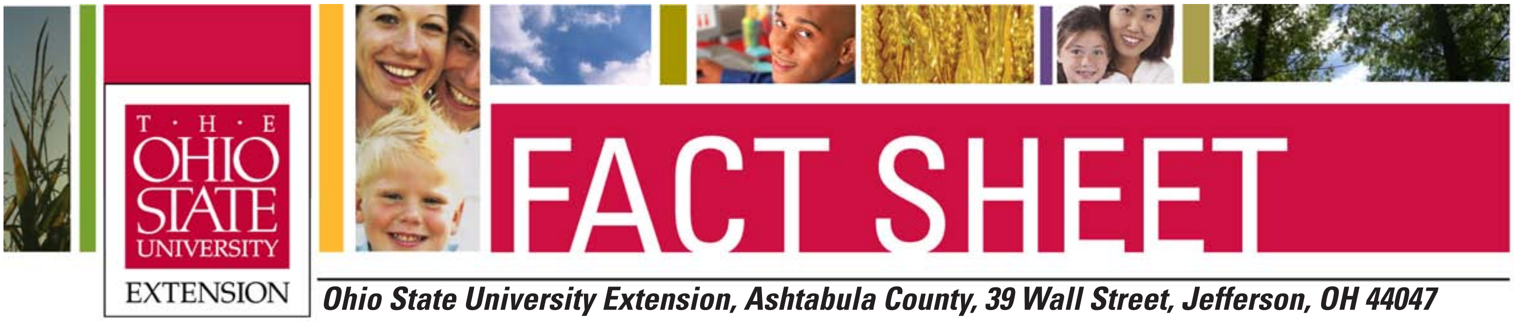

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"Building for the Successful Transition of Your Agricultural Business" Fact Sheet Series

Planning for the Successful Transition of Your Agricultural Business

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As the age of farm operators increases, transferring the ownership and management of the family business to the next generation will become one of the most important issues farm families will face.

While many farmers dream of seeing their legacy passed on to the next generation, many postpone initiating a plan for the transition of their business for a variety of reasons. Many claim that there is not enough time to discuss these matters. Or if planning does occur, it simply involves the senior generation drafting a will describing how the farm assets should be divided among heirs.

Age of Ohio Farm Operators

Year	Age of Principal Operator
2002	53.8
1997	52.5
1992	52.0
1987	51.1
1982	49.8
1978	49.4
1974	50.5

Source: Census of Agriculture, NASS

The main question that the principal operator of a farm or agribusiness should ask is:

"Do I want to pass my farm operation to my heirs as an ongoing business or do I want to pass it on as a group of assets?"

If asset transfer is the goal, then an estate plan can be developed to determine who will get what, when they will get it, and how they will receive it. If the goal is to keep the business intact for the next generation, then a transition plan needs to be developed.

What Is Farm Estate Planning?

Farm estate planning is determining how farm assets *(i.e.,* land, buildings, livestock, crops, investments, land, machinery, feed, savings, life insurance, personal possessions, and debts owed to or by the farm) will be distributed upon the death of the principal operator(s).

What Is Farm Transition Planning?

Farm transition planning is the process by which the ownership and the management of the family business are transferred to the next generation.

The goal of transition planning is to make sure the business has the resources to continue for many generations. Transition planning helps the family analyze its current situation, examine the future, and then develop a plan of action. This includes planning not only for the transfer of assets but also managerial control. It should also include developing a strategy to meet the retirement needs of each generation.

Each farm family is different in regard to its goals for transition planning. Family dynamics, physical resources, financial position, and managerial styles vary from operation to operation. As farmers plan to transfer the family business to the next generation, there are a myriad of decisions to be made. One of the most difficult is determining how to be fair to off-farm heirs without jeopardizing the future of the heirs who have remained with the family business. Other decisions include deciding who will manage the business in the future, how to distribute assets, how and when the senior generation will retire, and how the business will deal with the unexpected.

No two transition plans are alike. Given the complexity of individual farm businesses and the unique personalities and characteristics of family members, a cookie-cutter plan, which families can adopt, does not exist. It is recommended, however, that the family address the issues presented here when developing the transition plan.

Determine If the Business Is Profitable

A business must be profitable in order for future generations to continue the operation. A comprehensive review should be conducted to determine the production, financial, marketing, and personnel management strengths and weaknesses of the business.

An excellent way to accomplish this is by conducting what is called a SWOT analysis. This analysis examines the Strengths, Weaknesses, Opportunities, and Threats of the farm operation. This analysis helps the business examine a variety of business performance indicators. Some of these indicators could include commodity productivity, farm efficiencies, debt structure, and the financial viability of the business.

(For information on how to conduct a SWOT analysis, refer to the OSU Extension Fact Sheet *Conducting a SWOT Analysis of Your Agricutural Business.)*

After completing a SWOT analysis, it is recommended that a comprehensive business plan be developed. This plan allows the family to develop strategies to meet the production, marketing, financial, risk, and personnel management sectors of the business. It can also include strategies for improving the financial position of the business so that multiple generations can be involved in the business. In short, the agricultural business plan presents a picture of the agricultural business or farm, where the business is going, and how it will get there.

Involve the Family

Transition planning is a process in which the entire family should have a role. It should not be about secret meetings between parents and the favorite sibling. Many operations utilize family business meetings as a strategy to involve the entire family in the transition process. It should be noted the underlying success of any business depends greatly on healthy family relationships and open communication. Many two-generation family business arrangements fail because of poor family communication and relationships.

Family business meetings can help the entire family communicate about sensitive issues. They can also allow the family to plan for growth so that multiple generations can earn a living from the business. These meetings also allow the family to develop a transition plan that complements the estate, retirement, investment, and business operation plans.

(For more information on conducting family business meetings, refer to the OSU Extension Fact Sheet *Conducting Family Business Meetings.)*

Develop a Plan to Transfer Assets

Planning how to transfer the tangible and intangible assets of the farm operation should also be addressed in the farm's transition plan. In most cases, these plans are made and executed through the estate plan, which is initiated upon the death of the principal operator. However, a business can also transfer many of these items to the next generation prior to the death of the principal operator.

Tangible items include things you can touch such as breeding livestock, crop inventories, machinery, equipment, land, and buildings. Rarely does the next generation take over ownership of all the tangible business assets at once. Usually ownership is assumed as their experience and commitment to the business increase. These assets can be transferred through gifts, sales, or through the estate or a trust upon death. Due to the potential tax implications of transferring these assets, consultation should be with an attorney and tax practitioner, each having experience in transition planning.

The intangible items that should be transferred are sometimes less obvious, but they are just as important when developing the transition plan. Intangible items can include verbal agreements, goodwill, authority, and location of records. The senior generation should invest the time necessary to transfer their knowledge of these items to the junior generation. For instance, there may be many unwritten arrangements with neighbors or with suppliers of feed, seed, fertilizer, or veterinary services. The primary operator also has historical information that should be shared with the next generation. This could include well and tile placement, electrical wiring, and the location of legal documents vital to the operation.

Other discussions should center on when the next generation is or is not authorized to obligate the farm (buying a tractor or other expensive capital items) and when the next generation will take over control of certain activities such as paying bills and keeping production or compliance records.

Develop Future Managers

Transferring assets to the next generation is often easier than transferring management. Many family farms have two to three generations working side by side. Farm families traditionally operate in a hierarchical structure where the older generation holds the purse strings until death. Oftentimes, the junior generation is not given any managerial control until its members are old enough to retire themselves. Farm businesses should develop a plan for sharing managerial responsibilities between generations and anticipate management voids created by people moving up, retiring, or leaving the business.

Development of managers is a long-term investment in people and should not be ignored. Many excellent community and Extension management courses exist in which the junior generation can enroll to increase its managerial skills. The senior generation should not wait until death or a few months before retirement before transferring control. The transfer of managerial skills should be treated as a process, not as an event.

Develop Plans for Retirement

No one expects to work forever. Each generation should develop an individual retirement plan, and the business should help family members meet their expected retirement needs. The two main retirement questions that will need to be addressed are how much money does each family member need for retirement and what will the farm obligation be to retirees?

A variety of factors such as age at retirement, retirement housing, and other retirement accounts held by the family will affect the amount needed for retirement. It is important that the profitability of the farm be such that a family member can retire and not adversely affect the financial position of the business. In some cases, the farm business has to be sold in order for a senior member to meet retirement needs.

Develop Contingency Plans

Successful businesses also recognize that life is full of twists and turns. Given this, attention should be given to the unexpected. Contingency plans should be made for when key managers leave the business unexpectedly or when unplanned events such as death, divorce, disability, and health problems arise. Each of these unexpected twists could damage the viability of the operation if contingency plans have not been made.

Develop a Timetable for Implementation

It doesn't happen all at once. A timetable should be established for accomplishing each step in the transition process. Without a timetable, you won't know if you are failing or succeeding in hitting your objectives. Many families will utilize a testing or a probationary period for the transfer of ownership, management, income, and labor. Given the complexity of most farm operations, the transition process could take years.

Final Thought

Transferring a family farm or farm business to the next generation can be a challenging task. Legal issues, tax laws, and personal differences between family members are some of the issues families must confront when deciding how to transfer the managerial and asset control of a family business. Working together, families can answer the tough questions and develop a transition plan that will provide the opportunity for the agricultural business to be successful for many generations.

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