2011

Land/enterprise and ownership transfer

Lucy C. Meyring
Walden, Colorado

Proceedings, The Range Beef Cow Symposium XXII
November 29, 30, and December 1, 2011, Mitchell, NE

Land/enterprise and ownership transfer

Lucy C. Meyring
Walden, Colorado

YOUR ESTATE PLAN MAY BE THE DEATH OF YOU YET!!!!

*****The average age of America's farmers and ranchers is 55

*****There are twice as many farmers over the age of 65 as under the age of 35

*****Half of agricultural land is owned by folks older than 75

*****69% want to pass their farms or ranches on to their children

*****Only 3-5% of farm and ranch families in Colorado have a complete estate plan

*****The Family Farm Institute reports that only a third of all family businesses succeed in the second generation and a mere 15% survive to the third and 5% make it to the fourth.

*****Statistics indicate the number of cattle operations has declined 20 percent since 1981

*****As inflation rises and land values go up, more land and livestock are needed to support a family

*****AGRICULTURE SHOULD BE PUSHING FOR INFLATION INDEXING. To tax the full capital gain is wrong, because much of the value is the result of inflation.

*****The Death Tax is a government seizure of family owned and operated businesses

*****By splitting up and destroying viable farming and ranching operations, the death tax erodes the base of the rural economy

*****The death tax accounts for only 1 per cent of federal revenues

*****Research indicates that:

42% of the first generation farm families have not discussed the subject of farm succession with their spouses;

63% of the first generation have not discussed succession with the second generation (their own children).

Only 16% had included the son or daughter in conversations about succession.

Most older generation farmers and ranchers, surveyed, indicated that "the farm" would be the source of their retirement income.

SUCCESSION PLANNING

STAGES IN THE AVERAGE PERSON'S FINANCIAL LIFETIME:

1. Working to pay off debts.
2. Assets in land, livestock, and equipment grow.
3. Building a retirement portfolio.
4. Making provisions for the future of the business.

One of the most difficult decisions family businesses face is planning for succession. If the business is to survive, it is critical a plan exists that allows for the next generation to gradually assume responsibilities and accountability.

STAGES FOR IMPLEMENTING A TRANSITION PLAN ON A FAMILY FARM OR RANCH:

1. "Dating" period. Allows for the successor and current operator to try out the arrangement on a trial basis for a period of time. Mentoring is crucial. Many responsibilities are learned as an employee—usually a wage is paid during this period.
2. Start sharing in some duties. It is time for commitment on the part of the successor.
3. Eventually take over some of the duties being performed until the successor is ready to take over the business. Senior members may opt to begin transferring percentages of the business or selling discounted shares to the successor for either cash or promissory notes at a low, legal interest rate.
4. Retiring generation allows someone else to take over the management; however, insuring that they themselves are financially secure.

WHY SOME FAMILIES DELAY TRANSFER:

*****Fear about losing one's identity;

*****Fear about loss of purpose upon retirement;

*****Anxieties about financial security;

*****Wanting to pay the debt off before handing the business over to the children;

*****Lack of confidence in next generation;

*****Being fair to all children;

GETTING STARTED WITH A SUCCESSION PLAN:

1. Make your mind to begin planning. Bringing in another person takes an estimated $150,000 to $250,000 in gross revenue, or $40,000 to $70,000 of net profit.
2. Transitions are twice as likely to be successful and the business four times more profitable when the family member works for someone else for three to five years.
3. Move the successor into management and decision-making within six years. Farms that fail to do so are twice as likely to have an unsuccessful transition and are less profitable.
4. Don't stay too long before turning over the business and losing your cutting edge. The optimal time for ownership and management of a business is 30 to 35 years.
5. The most successful transition plans have the business assets transferred to those managing the business. There is a difference between treating people fairly and treating them equally. (Children working the operation vs. children not involved in the operation).
6. An operating agreement should include time expectations, goals, responsibilities and accountabilities.
7. A transition plan that covers dissolution of the business is critical. Plan for risks: Death, Divorce, and Disagreements. Have a good buy/sell agreement in place.
8. A list of advisers should include a lender, a lawyer, an accountant, a financial planner, spouses and all partners. Hold at least one annual team meeting. COMMUNICATION IS KEY!!!
9. Develop a true net worth statement including realistic market values of assets and liabilities.
10. Set your goals. Sit down with your spouse and decide what's most important to you. Each generation has different values. Yours may not coincide with your heirs.
11. The biggest concern with family business transition plans is procrastination. A plan often takes 2-3 years to formulate.
12. Revisit the plan periodically to take in to account any new births, divorces, etc.

TOP TEN THINGS FAMILIES DO TO BRAK UP THEIR

RANCHING OPERATIONS

1. Assuming all genetic relationships equal good working relationships.

   Because people are members of the same family does not mean they will automatically have the same ideas and values or they will want to do the same things. In many families the best way to create harmony is to ensure family members don't work together.

2. Believing the business can financially support any and all family members who want to join.

   A. Can the business support more than one family household;
   B. If it can, are the family members who intend to join the business suited to the business, if yes, is the business suited to the family member.

3. Assuming everyone involved will be willing to make changes. It is natural for people to resist change initiated by others.

4. Presuming a conversation is a contract.

5. Believing mind reading is an acceptable form of communication.

   Learn to share the complete picture. Example: Location of a fence line, moving cattle, etc.

6. Failing to build communication skills and business/family meeting tools when the times are good so they'll be in place to use when the times get tough.

   In good times if communication is lacking it doesn't present such a problem; however, when things are going badly (difficult times in the industry, low prices, drought, or problems with a family member), the lack of communication can cause real friction within a family.

7. Ignoring the in-laws, off site family and employees.

   Individuals not involved in the day to day communication may start to imagine all sorts of negative things are happening. These can be mostly imagined, but the absence of inclusion means exclusion and the imagination runs wild.

8. Forgetting to use common courtesy. Treat one another with love and respect.

9. Having no legal and discussed, management transfer plan or buy-sell agreement.

10. Failing to celebrate.

KEY STEPS IN AGRICULTURAL ESTATE PLANNING

1. Transfer Ownership (if one so chooses).

   The primary goal of estate planning is to facilitate the transfer of ownership and management of the ranch, business and other assets. Estate planning ensures that the ranch will be passed along to the intended party with as few complications as possible.

2. Reduce Estate Taxes and Avoid Unnecessary Transfer Taxes.

   Planning the estate with the help of a qualified professional team will help limit the taxes the estate has to pay.

3. Secure Financial Futures for the Senior Partners

   The Estate can be set up so that the costs of medical care, funeral, and settling the estate are covered by the estate, rather than its beneficiaries.

4. Develop Management Skills For the Next Generation

   Choose the business ownership structure and asset transfer methods that allow the younger generation to participate in the management and ownership of your ranch as soon as both generations are ready.

5. Leave a Legacy.

   Ultimately, the senior partners must make the final decisions regarding an estate plan. They are the ones who have worked hard to increase the value of their businesses—it is their property and, as such, they have a right to own and dispose of it as they deem appropriate. Parents do not "owe" their children an Estate, but they do "owe" them a discussed, legal estate plan and the tools to help them with the details after they are gone. Many children feel "entitled" to an inheritance. Hopefully, open communication will lead senior partners to a plan that is fair and promotes harmony among the heirs.

"IF YOU LEAVE THE RANCH FOR YOUR HEIRS TO FIGHT OVER, AND THEY END UP SELLING IT TO SETTLE MATTERS, WHAT KIND OF LEGACY IS THAT?"