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# Guide to Succession Planning: Passing on the Farm



## Protect Your Assets, Heirs and Heritage

Succession is about more than planning the future of the farm. At its heart, succession planning is about preserving an agricultural legacy and the heirs who inherit it. The process often focuses on leaving the farm to your children and preparing them to succeed as the next generation of operators and stewards of the land. The notion, while romantic, is not always simple—especially if you have multiple heirs.

“A lot of farmers don’t want to treat farming children with any preference [over non-farming children], but that doesn’t bode well for the future of the farm,” explains Dennis Stein, farm management senior educator at Michigan State University. “For succession planning to work, you have to make a decision to treat farm kids different than non-farm kids.”

In succession planning, experts urge farmers to embrace the notion that fair does not mean equal; the distinction, according to Stein, is essential to safeguarding the future of the farm. The reason: There is a risk that non-farming children might be more interested in cashing in on the value of the farm than preserving it, causing conflict with the heir who wants to continue farming.

“The heirs with no ties to farming can become uncooperative or hostile to farming partners,” he says. “A consensus to move forward to operate smoothly isn’t going to happen.”

When it comes to protecting your heirs, assets and the future of the farm, there are five things to consider: >>



## 1. Splitting farming and non-farming assets between heirs

In this scenario, all farming assets, including land, equipment and livestock are left to farming heirs, while assets outside the farm business, including insurance, retirement accounts, off-farm savings, mineral or oil rights, and rental/vacation properties go to off-farm heirs.

The value of the farm assets might be greater than non-farm assets, but it gives farming heirs full control of the land and operations to pursue their livelihoods and maintain the farm. It's a classic "fair but not equal" scenario.

"We want to be fair, even if it's not equal, because we know the sweat and toil and sacrifice associated with working the land," explains Kevin Bearley, an attorney specializing in agricultural law with the Colorado firm K•Coe Isom.

## 2. Dividing the farm

If there are multiple farming heirs who cannot work together, Elaine Froese, farm coach and author of *Do the Tough Things Right: How to Prevent Communication Disasters in a Family Business*, believes it's better to separate the farm into separate entities and let each heir control their own (smaller) farm.

It might be difficult to imagine dividing up the farm, but it's a better option than risking the dissolution of the farm over time because the heirs can't agree on how to run it.

## 3. Addressing life's uncertainties

Succession planning requires working through—and planning for—multiple scenarios, including unexpected death. A solid plan also minimizes the likelihood that fractured relationships will wreak havoc on the farm.

"Relationships are complicated," notes Robin-Lee Norris, partner in the Guelph, Ontario, office of the Canadian national law firm Miller Thomson LLP. "Divorce, cohabitation and kids from previous marriages all need to be considered in succession planning."

Preuptial agreements, Norris believes, are essential to protect farm assets from unintentionally ending up in the hands of ex-spouses. Corporate shareholder agreements can also be written to prevent spouses or other family members from accessing shares of the family farm.

## 4. Minimizing tax burdens

A USDA Economic Research Service report found that farmers were more than twice as likely to owe federal estate taxes than non-farmers (and owners of commercial farms are 10 times more likely to owe estate taxes than small farm owner/operators).

To preserve farm assets, Bearley recommends using gifts and trusts in tandem. The best option: Establish a trust and make gifts (like land or equipment) to the trust, which protects your heirs and farm assets. (For more information on the tax liabilities of and limits to annual monetary gifts, see "Farm Succession: A Case Study.")

"Trusts benefit heirs, because they can't sell or lose gifts or assets that are placed in the trust," he explains.

Bearley favors Intentionally Defective Irrevocable Trusts (IDITs), which allow farmers to sell assets to the IDIT in exchange for a note, freezing the value of the estate with no gain/loss on its sale and no tax on the interest payments received on the note.

IDITs, which have been around for decades, are, according to Bearley, "The only way I know to protect land for multiple generations."

## 5. Planning for retirement

Handing off the farm means you're giving up the income—and perhaps the homestead—that came with making a living as a farmer. The ongoing need for income into retirement must be addressed through succession planning, according to Stein.

"One of the biggest questions is, 'How do I fund my life if I'm not a farm owner/operator?'" he says.

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**Order it** [Click to order Elaine Froese's guide to family communication.](#)



**Read it** [Click to read "Farm Succession: A Case Study" online.](#)



One of the advantages of creating a succession plan a decade (or more) before transitioning off the farm is the ability to plan for a successful retirement. With the help of your succession planning team, including a lawyer, accountant and financial planner, ask these questions:

“At each step of the process, you must make sure that you have what you need for ... the future viability of the farm.”

**HAVE I SAVED ENOUGH FOR RETIREMENT?** Use a retirement calculator to run the numbers. If you're not saving enough for retirement, is it possible to allocate extra contributions to retirement accounts like IRAs or RRSPs? It's essential to examine the options for addressing the shortfall. The possibilities, according to Bearley, include remaining a shareholder on the farm or renting the land to farming heirs to keep income flowing.

**WHERE WILL I LIVE?** You might be planning to stay on the farm; if farming heirs need to move into the house, will you buy or rent a new home? In Ontario, for example, building a new home on the farm (called a retirement lot) is prohibited, forcing farmers off of their land if heirs move onto the farm. As with all matters concerning succession, check the laws where you live to understand your options.

If there are no farming heirs, you can establish a tax-free 1031 real estate exchange that allows farm property to be exchanged for property, including a home.

**HOW WILL WE PAY FOR LONG-TERM HEALTHCARE?** The U.S. Department of Health and Human Services established a website ([www.longtermcare.gov](http://www.longtermcare.gov)) to explain Medicare coverage, the costs of long-term healthcare and options to purchase insurance. In Canada, the Canadian Life Health Insurance Association has a guide to supplemental health insurance on its website ([www.clhia.com](http://www.clhia.com)) and provincial programs may help with the costs of prescription drugs and other long-term healthcare needs.

Froese acknowledges that succession planning requires asking difficult questions and engaging in uncomfortable conversations. In fact, farmers often avoid preparing for succession because the process is stressful.

Throughout the process, your succession planning team will help you make informed decisions; as the farm founder and/or current owner, it's essential to engage in the process to ensure your assets, heirs and heritage are protected.

“At each step of the process, you must make sure that you (and your heirs) have what you need for economic security, family harmony and the future viability of the farm,” she says. **FL**





## The Basics

After farm chores are done, there is often just enough time for a hot meal and hotter shower before turning out the lights and heading back to the barn in the morning. Carving out time for succession planning falls to the bottom of the to-do list (again), which doesn't bode well for the future of the farm.

“Succession planning is an integral step in the strategic planning of a farm business,” notes Nicholas Betts, business management specialist with the Ontario Ministry of Agriculture, Food and Rural Affairs.

Although a succession plan is important for a successful farming operation, it can be overwhelming to get started, which is one of the reasons 73% of American farmers and 70% of Canadian farmers haven't identified a successor or created a succession plan.

Think of succession planning like raising a crop: It doesn't happen overnight and requires a lot of small steps from seed to sale. Follow the steps on the next page to get started on a succession plan for your farm. >>



# 8 Steps To Get Started



“Succession planning always starts with a conversation.”

## 1. Schedule a family meeting.

Succession planning is a team sport. It requires input from the entire family, including current farm partners, as well as your children and their spouses.

“Succession planning always starts with a conversation,” says Elaine Froese, farm coach and author of *Do the Tough Things Right: How to Prevent Communication Disasters in a Family Business*.

During family meetings, Froese suggests talking about a target retirement date (even if it’s a decade or more down the road) and goals for the future of the farm. Understanding how all of the stakeholders feel about passing the farm to the next generation is an essential first step in succession planning.

If needed, bring in a farm coach/advisor to facilitate the process and keep the conversation on track.

## 2. Assemble your team.

You’ll need experts to facilitate various steps of the succession planning process, including offering advice on the legal and tax implications of various decisions.

“One of the upsides of having a team is access to options and the best ideas,” says Kevin Bearley, an attorney specializing in agricultural law with the Colorado firm K•Coe Isom. “Sometimes [advisors] don’t communicate well with each other and can’t agree on the best option.”

Choose advisors you like and respect, and who, ideally, work well together (perhaps several experts from a single firm) and prepare to have them involved throughout the process.

## 3. Establish goals for succession.

Think about a target date for retirement and the steps that need to happen between now and then. Those steps might include the phased transfer of labor, management and assets; training/mentoring the next generation; a financial plan (to fund retirement); and plans for contingencies that might arise between establishing and executing the succession plan.

“If you want your farm to continue to be an operating farm [after you retire], it’s important to think about your goals for the future of the farm,” Betts says. “[You have] to make sure such a transition is possible and successful.”

Ask the stakeholders (current partners, farming and non-farming heirs) about their goals for succession. If there are discrepancies, take time to work them out.

Disagreements, Betts explains, “can cause significant stress and conflict in the business and farming family.”

## 4. Make a list of assets.

As part of the transfer of ownership from one generation to the next, it’s important to know which assets need to be accounted for in the purchase/sale, or included in the trust or gift.

In addition to listing assets, include a note about who owns them: Do you own 100% of these assets? Are there partners or shareholders who own a portion of them? This information is essential to share with the advisory team, who will use it to create a plan for transferring assets to the next generation.

Your list should also include non-farm assets, including retirement accounts, rental/vacation properties, life insurance and investment vehicles not tied to the farm, according to Robin-Lee Norris, partner in the Guelph, Ontario, office of the Canadian national law firm Miller Thomson LLP.

“Most farms are asset rich and cash poor,” Norris notes. “You need to know what you have to help plan for the future on and off the farm.” >>





## 5. Make a list of debts.

Debt is also an important element of succession planning. If assets are still being financed, you'll need to put a plan in place to pay them off or establish financing agreements for the next generation to take over the debt.

There is another reason it's a good idea to assess the overall financial health of the farm, according to Heather Watson, executive director, Farm Management Canada. "In a debt position or down market, the farm may be a burden or liability for the next generation, not an opportunity," she says. "If there is more debt than assets, farmers have to ask if the farm is worth passing on."

## 6. Gather existing documents.

To help get a complete picture of the farming operation, your advisors will want to know what documents already exist as a starting point for succession planning.

Assemble any shareholder agreements, life insurance policies, wills or trusts, durable power of attorney and healthcare directives for the team to review and update if needed. If you have a previous and/or outdated succession plan, include that too.

"Your succession plan needs to be reviewed on a regular basis," Norris says. "If it's out of date, it might not reflect current goals or regulations."

## 7. Agree on a timeline.

Transfer of ownership and assets from one generation to the next doesn't happen overnight. As part of the planning process, agree on a tentative timeline for succession. Remember: It can take a year just to get a plan in place and up to a decade to fully execute a succession plan.

"It's a good idea to start early and do it a little at a time," Norris says.

Betts agrees that establishing a realistic timeline (advisors can help make recommendations for the ideal transfer of assets and operations) and taking it slow is best. Rushing to complete a succession plan, he explains, "can lead to financial loss, equity loss, or worse, family conflict and crisis."

## 8. Take action.

Once all of the pieces are in place, it's time to work with the team of experts to create a succession plan and begin implementing it—and this can be one of the hardest parts.

"People get stuck at the implementation phase," explains Froese.

To keep the succession plan from sitting on the shelf, Froese suggests allowing the most passionate member of the farm family to take the lead and help drive the process.

"There is an old Japanese proverb, 'Talk does not cook rice,'" she says. "It's the same with succession planning. You can't just talk about it, you have to take action." **FL**



“It’s a good idea to start early and do it a little at a time.”





## Know Your Options

Even if succession seems straightforward, as when passing on assets and operations to a single heir, multiple steps are still required to create a plan to facilitate the transfer of the farm from one generation to the next.

The succession planning process may require changing business structures, deciding between rollover, direct sale or placing assets in a trust. In more complex cases, it might make sense to divide farming operations, enter into a contract with an outside farmer or sell the farm.

“I wish I could say there is a one-size-fits-all approach, but it’s just not the case,” notes Robin-Lee Norris, partner in the Guelph, Ontario, office of the Canadian national law firm Miller Thomson LLP. “It’s complicated.”

Because of a succession plan’s complex nature, a team that includes a lawyer and accountant is indispensable in helping evaluate the legal and tax implications of different business structures and vehicles, like trusts, used to transfer assets and operations. A professional team will also complete the paperwork required to prepare a formal succession plan.

### Evaluating Operations

Once your family has established goals for the future of the farm, including an estimated retirement date, and a plan to transition operations and assets, your advisors will look at the current business structure and determine whether it can help you meet those goals or if restructuring is needed.

Each business structure—sole proprietorship, joint venture/partnership and S-Corp—has its own advantages and disadvantages, and each will have an impact on taxes, liabilities and the ease of transferring assets in and out of the farm business.

**SOLE PROPRIETORSHIP:** Although this is the simplest and most common business structure, according to the U.S. Small Business Administration, it also carries the most risk. A sole proprietor owns and operates the business as an individual; the proprietor receives all of the profits, but is also responsible for the debts, losses and liabilities the farm business incurs.

**PARTNERSHIP:** A partnership refers to a single business with two or more owners (partners). The partners share responsibilities for all profits and losses. A joint venture is a form of partnership that is created for a limited period of time or specified project. On a farm, for example, one partner might own land and the other owns the equipment (as separate businesses), while operating a joint dairy-calf operation. Joint ventures offer some liability protection and the ability to put assets into the farm (or pull them out) without incurring taxes. Another partnership option is a limited partnership, which allows partners to minimize their liabilities and take responsibility for varying degrees of input on management decisions based on their share of the business.

**S-CORPORATION:** Often called an S-Corp, it’s a separate legal entity that separates the corporation from its owners/shareholders. The corporation is formed through the IRS. An S-Corp offers tax savings, tax credits and liability protection, but it’s also subject to stricter operational processes, such as scheduled shareholder meetings, adoption of by-laws and additional record-keeping.

The right business structure for your farm depends on a number of factors, notes Kevin Bearley, an attorney specializing in agricultural law with the Colorado firm K•Coe Isom. The decision to restructure is best made with the help of an accountant and attorney.

In general, Bearley recommends farmers establish partnership agreements. “Partnerships let us separate land from farm operations and allows operations to be >>

“I wish I could say there is a one-size-fits-all approach, but it’s just not the case.”





placed with the partner who's farming," he explains. "Having all of the assets tied up in one business entity can cause problems."

For the purposes of succession planning, a partnership structure, Bearley explains, gives farming heirs control of the operations, including the freedom to maintain the farm, purchase equipment and make decisions about operations without interference from their off-farm siblings, who own the land (and often receive rent from their siblings who farm it).

In Canada, there are fewer options for structuring businesses, according to Norris. For larger farms, Norris recommends farmers create corporations with strong shareholder agreements to provide protection against lawsuits; smaller farms, she says, might find partnerships more advantageous (the pros/cons of different business structures are essentially the same on both sides of the border).

## Crafting a Plan

After the business structure is evaluated (and restructured, if needed) the next step is creating a plan for how operations will be transferred and who will take over the farm.

Dennis Stein, farm management senior educator at Michigan State University, recommends transferring ownership in phases, following these three steps:

- 1. HAND OFF ASPECTS OF FARM MANAGEMENT:** Giving farming heirs additional responsibilities will help prepare them to take over farm management when the founder(s) retire. Consider dividing up livestock from cropping operations, for example, and letting the farm heir run a specific aspect of the farm business.
- 2. CONVERT FARMING HEIRS FROM HOURLY WORKERS TO PARTNERS:** As their responsibilities increase, farming heirs should be rewarded with additional compensation, including a salary and performance incentives.
- 3. START TRANSFERRING ASSETS:** In preparation for succession, encourage farming heirs to begin acquiring assets or start transferring assets into their name/business. For example, when the farm needs a new tractor or the 40 acres next door comes up for sale, your heir, not you, should make the investment.

“The decisions become very hard.”

“Implementing a succession plan over time is a much more stable method for the future of the farm,” Stein explains. “As farming heirs prepare to take over the farm, they’ll need help from senior generations to acquire the assets and make a smooth transition.”

The phased transfer of ownership from a farmer to a single heir is one of the more straightforward aspects of succession planning. The process becomes more complex if there are multiple heirs, including a mix of farming and non-farming children, or no heirs at all.

“The decisions become very hard,” Stein says. “There is a risk that the farm could get chopped up into small pieces or operate with a whole group of partners, including some with no ties to farming, who can’t reach a consensus about how to move forward.”

## Embracing Alternatives

Although the options might be less straightforward—and less obvious—when there are no heirs or multiple heirs with differing interests in the farm, there are solid options.

To accommodate multiple heirs in a succession plan, scenarios could include separating farming and non-farming assets between heirs (giving land, equipment and livestock to farming heirs, then giving rental properties and mineral rights to non-farming heirs, for example); dividing the farm into multiple, smaller, operations; or selling the farm and splitting the proceeds. (For more on planning a succession for multiple heirs and anticipating uncertainties, see “Protecting Your Assets, Heirs and Heritage.”)

With no heirs, the land and equipment could be rented to a neighbor or a beginning farmer. Most states have programs that help new farmers access land, equipment and assets, like breeding stock through partnerships with retiring farmers. In some states, farmers are eligible for tax credits for renting agricultural assets to new farmers. You retain ownership of the farm as part of your retirement portfolio and the rent provides ongoing income. >>



For additional information about succession planning (and help creating a plan), check out these resources:

## United States

Purdue Extension  
extension.purdue.edu  
765-494-8491

Center for Rural Affairs  
cra.org  
402-687-2100

International Farm Transition Network  
farmtransition.org

K-Coe Isom  
kcoe.com  
970-685-3500

Dennis Stein  
Michigan State University  
msu.edu/~steind/  
989-672-3870

Gary Hachfeld  
University of Minnesota Extension  
extension.umn.edu/county/clay/extension/  
contact/gary-hachfeld  
507-389-6722

## Canada

Agricultural Institute of Management  
agr.gov.sk.ca

Farm Credit Canada  
1-888-332-3301  
fcc-fac.ca/en/

Robin-Lee Norris  
Miller Thomson LLP  
millerthomson.com  
519-780-4638

Elaine Froese  
elainefroese.com  
204-534-7466

Nicholas Betts  
Ontario Ministry of Agriculture, Food and Rural  
Affairs  
omafra.gov.on.ca/  
519-826-3173

Heather Watson  
Farm Management Canada  
fmc-gac.com  
888-232-3262

If there are no heirs, you could also donate the farm and equipment to a registered 501c3/nonprofit organization. This option allows you to avoid estate taxes, but doesn't guarantee the future of the farm or provide cash to fund retirement. A conservation trust, which can be structured to allow new farmers or heirs to acquire land at "agricultural value" or require land be kept in agricultural use, is also an option. As a last resort, the farm could be sold, but Bearley warns that there are disadvantages, including a significant tax bill, associated with selling off agricultural assets.

It can be expensive to assemble a team to make recommendations about an optimum business structure and plans for passing off operations to the next generation (or alternatives if no one wants to take over the farm). The price for creating a succession plan, according to Norris, ranges from \$10,000 to \$15,000 (or more).

Canadian farmers have access to funding to cover the costs of succession planning. Through Growing Forward ([www.agr.gc.ca](http://www.agr.gc.ca)), a program through Agriculture and Agri-Food Canada, farmers can access cost-share funding for advisory services, including succession planning. In the U.S., farmers have to absorb the cost as a business expense.

Regardless of the cost, Bearley believes investing in a succession plan is essential. "You don't work 30 to 40 years for it to all fall apart," he says. **FL**



  
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**editorial director** Richard Banks  
**creative director** Jamie Cole  
**contributing editor** Jodi Helmer

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