

# PLANNING FOR FARM SUCCESSION\*

Alan Miller and Craig Dobbins  
Purdue Extension

## *Step-by-Step Checklist and Action Plan for Management Succession*

This step-by-step checklist will help you (and your professional team of advisors) to decide where you are in the succession planning process. It also gives you an action plan of what you need to do along with helping to identify any gaps in your planning.

### **Step One: Gather Information and Ideas and Discover Expectations**

- Have you attended an introductory workshop or seminar to gather ideas on farm succession planning?
- Have you read general information on topics related to farm succession planning (newspaper articles, Iowa State's Two-Generation Farming Series, Key Financial Performance Measures for Farm General Managers, Transferring the Farm Series from the University of Minnesota, etc.)?
- Have you talked about the general issues of succession with family, friends, other farmers, and lenders?
- Have you selected a family member to lead the process (e.g. someone who will ensure things get done and timelines are set and followed)?
- Have you decided to involve/hire a facilitator (e.g. quarterback to help guide you through the process)?
- Have you started to look for an identify professionals who can advise you later in the process in regard to examining options, making decisions, and implementing your succession plan? An interview with likely candidates for this role at this stage can be a valuable information gathering activity.
- Have you completed a financial analysis of your present business? Does it have sufficient cash flow to meet today's financial obligations? Is it profitable and viable today? Is there sufficient income to support additional entrants? Will it continue to be financially viable in the future? Will new entrants increase financial risk?
- Have you looked seriously at the family living costs? Will there be any drastic changes in family living requirements over the next while (e.g. someone getting married, having children, building a house, etc.)
- Have you discussed everyone's expectations, objectives, needs and goals for themselves and the farm business?
- Has the family started to jointly assess the compatibility of everyone's expectations and objectives?
- Have you examined both the technical and human aspects of retirement, if retirement is a prominent element of the transition?
- Have you started to create processes to effectively communicate information and make decisions (e.g. family meetings)?
- Have you started to think about:
  - Transfer of ownership: What is fair and equitable to everyone?
  - Who will take over the farm? When? How?
  - Transfer of management: How are decisions made right now? How will that change? How will new managers be provided an opportunity to grow their skills?
- Have you acquired some basic knowledge and understanding of:
  - Methods of transfer
  - Financing a transfer
  - Tax implications
  - Legal implications

## Step Two: Generate and Examine/Evaluate Options

- Have you started to generate as many options as you can that address the various issues and concerns of family members and the needs of the business, such as:
  - How can the senior generation prepare for and secure their retirement?
  - What can you do to treat all offspring fairly and equitably?
- What about the following considerations? Which have the most appeal? Which still need to be addressed? What additional questions do you have?
  - Business Arrangements:
    - ~ Sole Proprietorship
    - ~ Partnership
    - ~ C or S Corporation
    - ~ LLC
    - ~ Joint Venture
    - ~ Multiple entities
  - If the option is to work together for a few years, then you need to look at management roles and responsibilities (how will decision-making responsibilities be divided?); division of labor; how will successor skill development take place? Which has the most appeal: a spin-off, superfirm, or landlord-tenant? Each has different implications for roles and responsibilities.
  - If working together, various options for the form of the farm business agreement need to be considered, like:
    - ~ Gross Income Sharing Agreement
    - ~ Net Income Sharing Agreement
    - ~ Rental Agreements or other types of Agreements
    - ~ If the proposed business arrangements will involve intra-family/entity rental arrangements, have you worked out the details of those arrangements such as how the rent will be determined?
  - Financial Options (both internal and external)?
  - Retirement Issues (Where will money for retirement living and expenses come from? What activities will the retiring generation take part in to remain vibrant? Will the retiring generation remain involved in the labor/management/ownership of the family farm business?)
  - Insurance needs (life, liability, and disability)?
  - Have you integrate the management succession/property transfer plan with personal estate plans?
  - Have you developed dispute resolution mechanisms and a game plan for contingencies?
  - Have you developed an exit plan including buy-sell agreements for co-owners of property?
- Who will the successors(s) be? How will management and labor be transferred?
- How will ownership be handled? Including the actual asset ownership, purchasing, utilization, renting, gifts, bequests, etc. of assets (e.g. options for control and use of equipment and machinery, land and buildings; control along with productive assets like crops, livestock, quota, etc.)
- How do you want to involve off-farm family members, if at all?
- How do you want to treat non-family employees, if applicable?
- If you have a proposed plan where are you at in terms of obtaining buy-in from parties at interest?
- Have you started to write out the plan?
- Have you started to think about establishing a tentative timeline for implementation?

## Step Three: Make Preliminary Decisions and Check with Experts

- Have you started to use your list of options to make preliminary decision about ownership? Management control? Retirement? Succession?
- Have you started to put together a very rough draft incorporating some of your options?



Note: If you do not have a list of options, it might be worthwhile to take some time to work through Step 2 again. Often the most creative options emerge only after the most usual options have been identified.

- Have you assembled a team of succession planning professionals (e.g. an accountant, a lawyer, a lender, a financial/retirement planner, an insurance specialist, a family business consultant, FSA farm payment limit eligibility advisor, etc.) that you feel comfortable with and will be able to work with in developing and implementing your plans?
- Do your preliminary proposals resolve those recurring issues in family business transfer planning which surfaced during the process of discovering expectations and examining options?
- Now that you have a good idea of what you might like to do it is a good time to start visiting with the members of your professional team. They can provide invaluable assistance in terms of helping you understand the advantages and disadvantages of the options you are considering. Have you met with these advisors to vet the options you are considering and to identify additional or perhaps better options?
- Remember, this is your farm family's succession plan. You need to be in control and lead the process.

## Step Four: Decide on a Plan and Develop the Plan

- Have you created and written down some draft ideas and potential plans which incorporate your preliminary decisions into several possible approaches?
- Have you decided which plan would best achieve what family members would like to have happen to the farm business and estate?
- Have you reviewed the plan being considered with the family and asked for feedback?
- Have you sat down with each of your professional advisors and discussed your thoughts and plans to get their ideas? Keep going back until you are comfortable that your plans will do what you want.
- The team of expert advisors can review the plans and provide feedback, advice and comments as follows:
  - An accountant can give valuable advice and suggestions on tax implications of certain strategies and make suggestions on how best to handle specific transactions.
  - A lawyer can review and give advice on the legal ramification of various agreements. The lawyer's legal drafting skills likely will be critical at this stage because agreements will need to be formalized, new entities created, etc..
  - A lender will (in most instances) be involved in providing finances and financing options regarding how ownership transfer (purchase and transfer of assets) should take place.
  - A financial planner can help with planning both personal and business savings and investment strategies as well as addressing retirement savings issues.
  - An insurance specialist can look at how life, disability and other types of insurance can be utilized as part of the overall plan.
  - The business advisor and/or quarterback (can be one and the same) can have a look at the strategies and advice from the other professionals. He/she can help clarify items if there is any confusion or major changes suggested or needed in the plan. Professionals who specialize in

guiding family businesses through transitions of various types sometimes called family business consultants.

- A person who is knowledgeable about FSA payment limit eligibility rules is absolutely critical for many farm businesses because any change in business structure can have important implications for continued eligibility for the government program. Don't make a change in your business structure without running it by such an individual.
- Has the family farm management team sat down with the professional advisors as a "team" to discuss the various components of the plan in an integrated fashion? Don't let a "piecemeal" approach to consulting with advisors endanger the plan. If you visit with advisors separately, then it is your responsibility to keep all of them in the loop and current on where the plan is at and its provisions.
  - Have you taken the advisor's ideas and advice and incorporated them into your plans?
  - Have you finalized the plan? Is it written down?
  - Does your succession plan contain the following elements:
    - A retirement plan? (It should address financial requirements, travel plans, emotional needs, social and physical activities).
    - A plan for transfer of management and labor?
    - A plan for transfer of ownership, including up-to-date wills that are consistent with the transfer provisions of the business succession plan?
    - A contingency plan (e.g. death, divorce, disability, health problems, etc.)?
    - An exit plan? Someone once said, "You need to start a business with the end in mind."
    - A time table for implementation?
  - Have you thought about whether the plan addresses the differing needs of those directly affected by it, e.g. on-farm versus off-farm heirs and perhaps even future generations of the family?
  - With the previous question still in mind, have you thought about whether the plan has sufficient flexibility to allow for changes in the future?
  - If the plan creates new business entities, how easily/inexpensively can they be unwound if necessary?
  - Once all of the parts have been reviewed and revised, the family needs to come back together and have a final review and make a decision.
    - Ensure all family members (farming and non-farming children) have a chance for final review and comments. This must be an open process.
  - Are you still procrastinating on a final decision?

## Step Five: Implement the Plan

- Do the parties at interest to the plan understand what will be required to fully implement it?
- Have any family members actually started to put the succession plan into action?
- What has been done? What still needs to be done? When?
- If the plan involves gifts, sales, or other property transfers have you transferred property?
- If the plan involves new business entities, have you observed the legal formalities associated with those entities? Avoid managing a business entity like your "alter ego."
- Do you have a timeframe, in the future, when you will review and make necessary adjustments?
- As part of the monitoring, there may be issues, concerns and challenges arise. The plan may need to be modified. Flexibility is the key.
- If something needs fine-tuning and updating, then go through the appropriate process to do so.
- Remember to give credit, where credit is due – enjoy your achievements.