

# 10 SUCCESSION PLANNING

There are ways that succession planning can be managed well to get the best outcome possible, but it takes effort, time and careful planning.

## 10.1 ISSUES TO CONSIDER IN THE SUCCESSION PLANNING PROCESS

- 10.1.1 Timing
- 10.1.2 People management
- 10.1.3 Financial capacity
- 10.1.4 Transfer of the business
- 10.1.5 Meeting processes

## 10.2 HOW DO YOU START THE SUCCESSION PLANNING PROCESS?



# 10 SUCCESSION PLANNING

The succession planning process of passing on the farm business to the next generation can either create or minimise one of the biggest risks to any farming family. If managed well, both family and the business can prosper. If not, then either family relationships or the business, or both, can break down. It is this risk that creates fear in dealing with this issue and many farmers by default delay dealing with this important challenge.

## KEY POINTS

- Succession planning is a process rather than an activity to be solved with one meeting.
- Good communication and being proactive are key to a successful succession planning process.
- It is possible to manage succession planning well.
- What happened with succession planning in the previous generation may not work for this generation, as each family is unique and each period in history is unique.

Succession planning refers to the passing on of both the farm management and the assets of the business from the older generation to the next. It is about attempting to satisfy the wishes and security of the older generation while also accommodating the wishes of the following generation. Succession planning is also referred to as 'transition planning' and 'business continuance'. Essentially, it is about maintaining a viable business as the 'baton' of the farm is passed from one generation to the next or about preserving the farm capital for the superannuation needs of the older generation.

Succession planning should be viewed as a process that takes time – sometimes several years - rather than being the result of one family meeting. Success in this process comes about from listening to each affected family member, understanding their wishes and feelings, and looking for a set of strategies that will help the farming family successfully complete their succession goals. It will take time and effort to both plan and implement. It is unlikely that one meeting will be enough to accomplish this goal.

Succession planning is like strategic planning in that it is rarely urgent and so other tactical and operational activities often take the focus of management. However, it should be given a high priority because of the time required, and the negative impact this process can have if done poorly and too quickly. A succession planning process has a greater probability of success if started early. The reward for proper succession planning is significant, especially if the alternative may be to end up in the courts, where rulings may see equity between family members prioritized over wider business aspirations and possibilities.

A number of constraints will also need to be identified, ranging from the financial capacity of the business through to the needs and wishes of the older generation who currently own and operate the family business. If the older generation do not know or do not wish to talk about their intentions for succession, any succession planning process is likely to fail. Having the older generation willing to commit to the process

of succession planning is the first and most vital step in this process. Once this is established, the following issues will need to be considered.

## 10.1 ISSUES TO CONSIDER IN THE SUCCESSION PLANNING PROCESS

Each family farming business is unique as it has:

- A separate family history (how the farm was passed on from the previous generation).
- Its own unique membership, with diverse personalities. Some people will get on and some will not.
- Its own unique financial circumstances and ability to accommodate new financial demands.
- Its own collective and individual family goals.

It is difficult to provide a 'recipe' to guarantee a successful succession planning process, although communication is essential. Some guiding principles and a checklist of other issues are provided to highlight areas that should be discussed. Other references that are useful are listed at the end of this module and can be found on the GRDC website.

### 10.1.1 Timing

It is important to consider the impact of timing on the effectiveness of a succession plan. A good reason to view succession planning as a process rather than a 'one-off' project is that families, goals and opportunities change over time. If succession planning is viewed as a one-off project, then it will be the best that can be done at that time. It may not be the best in five years' time, when things have changed. Families change with family members being added either by birth or through new partners, so the specifics of a succession plan will need to change over time. Once the initial succession plan has been developed, it should become

a 'living' document that is assessed periodically over time, to test if it remains relevant to accomplish the original goals. It is recommended that it should be reviewed perhaps every two to three years.

### A proactive or reactive process?

A **reactive succession planning** process is one where no planning has been put in place and the business transfer occurs only at the reading of the older generation's wills. By contrast, a **proactive planning process** is one that is put into place after careful consideration, years before the older generation moves out of the business and involves the whole family.

Reactive succession planning may be the approach taken by the older generation for a number of reasons: perhaps to retain total control of the process, to avoid difficult decisions or family confrontations. Whatever the reason, this approach usually leaves difficult decisions to be made by the next generation, which can threaten both the viability of the farm and family harmony. This management method is about 'picking up the pieces' when major family events occur, such as a death, divorce or disability. If a family member experiences divorce, only then is thought given to how the settlement will affect the family farm finances, how the management structure will change, and what future the farming business will have. Leaving the decision making this late means there is little choice in the outcomes that eventuate, and may result in significant changes to the family farming business.

Proactive succession planning is more challenging but has a greater chance of both preserving the family farm business and maintaining family relationships. It means the hard work is done well before the older generation's will is read out, and is likely to leave a well-organised and well-communicated succession plan.

Both the reactive and proactive approaches are used by farming families and are valid as succession planning approaches. However, thought needs to be given to the older generation's objective in succession planning, as this will determine which method is best used. It is essentially the strength of leadership that determines which style is adopted.

## 10.1.2 People management

The challenge in farming families is to separate the 'business' of farming from the 'family' of farming. Most farms began and continue to exist because of the family, and the aim of most succession plans is to preserve family relationships and business viability through the succession process. Unfortunately, due to the persistent declining terms of trade, many farm businesses have found it difficult to maintain the economic ability to have each, or sometimes any, of the children inherit a viable farming operation. Inheritance expectations and financial capacity may not match and compromises may need to occur.

It is good to focus on each family member's wishes, expectations and feelings, in an open and honest way, so that all understand each other, without prejudice. People are the most important part of the succession planning process and the most important skill is to actively listen to all involved in the process. This may be more easily said than done, as families often come with a history which can restrict effective listening.

As the older generation have put their working life into the business and usually own the assets, the most fundamental part of the succession planning process is for them to express their wishes as to what should occur. As they own the assets, they have the legal power and it is the distribution of this power that is so important to the success of the process.

### Inclusive or exclusive?

This approach to succession planning is similar to the previous section but it is more about treating succession planning as an open, transparent process that is inclusive of all those involved in the business.

**Inclusive management** includes being clear about processes, such as when a new family member joins the business, and ensures that the succession planning process is a topic always on the business agenda and is communicated clearly and regularly within the family business. Some of the following topics need to be addressed and guidelines developed for their management:

- > How will the families receive family drawings?
- > How does the current management team function, with roles and responsibilities defined?
- > How will the houses be owned, maintained and renovated, and at whose cost?
- > What is the succession plan, and how are all family members associated with it?
- > When a member of the business leaves, how are they bought out?
- > How will communication be maintained to enhance sound operational and tactical management?

This is a very proactive approach and will require good thinking and communication.

An **exclusive management** style in succession planning is one where the power is retained by the business owners, and intentions about business asset and management transfer are not communicated openly. This process excludes others and is not transparent, and may exacerbate poor communication and family relationships, and often leads to significant emotional stress. A significant factor often misunderstood by business owners who follow this management style is that it can actually be damaging to the business itself. A lack of transparency and trust in the succession process is probably indicative of a broader management style where the current business owner is closed to any input from others, which would eventually inhibit long-term strategic planning for the farm business.

### Rules of engagement

People and family are the most important part of the succession planning process and it is important to set the ground rules for any discussions. These will be unique to each family but could include decisions relating to the following:

- > Each family member be given time to contribute and be listened to actively.
- > Decisions are made either:
  - democratically,
  - by consensus, or
  - by the older generation.
- > Each family member will be valued.

- > The major goals and objectives will be determined by the family or older generation.
- > If general agreement cannot be met, how will decisions be made? Will it be the older generation who have the final decision?
- > All decisions are to be written down, to minimise confusion from relying on memory.

Communication requirements can differ between generations and by those who have partnered/married into the family. These should be acknowledged and discussed, so that everyone understands how the decisions will be made and implemented.

Negative family relationships can damage communication; it is important that each family member be gentle with and respect each other, so that the succession planning process has the biggest chance of success.

### 10.1.3 Financial capacity

Once the wishes of each family member are known, focus is needed on the financial capacity of the business to be able to deliver. This may require a number of different scenarios to be assessed (refer to section 11, **Analytical tools, Module 2**). P2PAgri, a farm business management decision tool will help with understanding where the business is currently and with assessing the scenarios to help make business decisions in support of achieving the objectives of the succession plan. This will assist all members of the family understand the current financial position of the business and the likely outcomes of the scenarios assessed. The financial constraints of the business will usually have a significant impact on the succession plan. However, this needs to be undertaken so all involved know how to manage the succession planning process.

### Farm business management planning

One area that helps succession planning is to clarify the current financial position of the farming business and who owns the various farm assets that will be subject to the succession plan. From this information, various scenarios that may have been suggested for the succession plan can be assessed. Budgeting tools to undertake a financial assessment of the business are available in section 5, **Module 2**. Analytical tools to explore the financial outcome of different management scenarios are discussed in section 11, **Module 3**. It is important to measure the financial capacity of the business and whether the chosen succession plan has a reasonable chance of being successfully implemented, or whether this becomes an onerous burden on those who remain in the family farm business.

### Ultimate goal

What happened last generation may not be possible this generation. One of the many challenges to family farms is that economic circumstances for farms have changed over time. So too have the expectations of farming families. What may have worked for a previous generation is unlikely to work with this generation. When discussing the options for succession, it should focus on what is possible given today's farm business financial capacity and the opportunity to access the aged pension, rather than what worked well 25 or so years ago.

### 10.1.4 Transfer of the business

Confusion occurs in succession planning when it is assumed that the transfer of management and asset ownership to the next generation happens at the same time, which does not have to be the case. In fact, succession planning happens more easily if these two activities are separated.

These two activities are usually referred to as:

#### Management transfer

- This is where management of the farming business is passed from one generation to the next. When you view the family farm as both a farming business and a real estate business, then it is easier to separate the activity of management. As has already been discussed in section 4, **Where is my farm business heading? Module 2**, management should focus on strategic, tactical and operational areas of business planning and management. The passing on of management from one generation to another can happen by staggering the transfer of management in these three areas over time, so that the next generation can gain mentoring and experience as they move through each stage. There are no ground rules here - each family needs to determine how this happens.

'I've got a son who's just become a part owner and partner in the business and I've got one permanent employee. I employ casuals at harvest time. Nigel does a lot of the day-to-day running and we discuss anything major. The final decision still comes to me a fair bit, but it's slowly getting less of that. It's a case of letting go really. We've now got it where Nigel and Susan own a third of the land and half the business and it's going pretty well. In the next few years, they'll buy another third which will give them control of everything.'

Brian Gregg,  
'Kolora', Emerald, Qld

The experiences of farming families who have successfully navigated a succession process highlight the use of two good principles in management transfer:

1. The next generation should gain some **responsibility for managing the farm business finances** before they reach the age of 30 years, so they can gain valuable experience in knowing what it is like to make decisions and spend money with uncertainty. That is, to spend money and learn what skills it takes to get more than that investment back. If the next generation are significantly older when they take over the financial management of the business, it could be harder for them to change from 'workman' mode to 'management' mode.
2. The next generation should earn the right to take over management rather than be given it. That is, the next generation needs to show initiative in gaining the

skills and experience needed to be a good manager. They need to put effort into their own management education and management skill development. If the next generation are given management without adequate practical experience, they may not be prepared enough to maintain a successful business.

### Asset transfer

- This is often referred to as **estate planning**, and relates to how the assets such as land, machinery and livestock are transferred to the next generation. It does not have to be all given over without liability or responsibility. If the older generation require financial security in their older age, there are ways that the next generation can cater for this. Estate planning normally relates to the writing of wills to distribute assets, but there are legal mechanisms that can be used to pass on the assets prior to a will being activated. This area is normally best discussed with a lawyer and accountant.

#### Fair or equal asset transfer?

A significant issue for many Australian farming families is the choice of being equal or fair when it comes to succession planning and asset division. 'Equal' implies each member of the next generation will have an equal share of the older generation's assets. 'Fair' means that given the desire to maintain the viability of the family farm into the next generation, the assets are allocated so that the farming business is secure and each child is recognised in a fair way, but perhaps with less than equal asset allocation.

This dilemma has been exacerbated by the decline in family farm wealth creation in recent decades, as the farmers' declining terms of trade have resulted in lower profits, and so the business' financial capacity to provide each child with a viable farm is severely restricted. In contrast, during the early 1900's, Australian agricultural land was still being cleared and was abundantly available. This enabled previous generations to provide additional viable farms for the next generation. In recent times, land prices have increased to such a high level that significant capital is now required for a viable farm, making the purchase of additional farms prohibitive. If the wish of the older generation is to pass the family farm on as a viable operation, then dividing the farm assets may not be an option, and non-farming family members would receive fewer assets.

Acknowledging this situation is important, and early planning is needed to cater for the non-farming family members. Non-farming family members can be rewarded using the following options:

- > Providing a good education to establish a non-farming career.
- > Establishing life insurance policies that provide life insurance payouts.
- > Placing land titles in their names that could be leased back to the family business.
- > Establishing off-farm investments that will become their assets in the future.

Knowing the intent of the older generation for handing on the family farming business, and communicating this with the next generation early in their life, improves the succession planning process. This is especially important, as it can significantly affect whether the farm is passed on as a viable business.

'Not all our kids are going to end up being farmers, so as a result of that, and being a very capital intensive business, we've got to work out a pathway that let's those that want to stay farming, farm, and those that don't, exit and go and do something else in a fair and equitable sort of way.'

David Mott,  
'Berryjerry Station', 'Wagga Wagga', NSW

### Risk management

A successful succession planning process needs to plan for how it is going to manage potential risks to the business' asset base. Two major risks that generally create barriers to a good succession planning process are:

- > The financial risk of **divorce**.
- > The issue of the **wills being challenged**.

How does the family protect the business from these risks?

#### Protection from Divorce

When the next generation start to find partners and bring them into the family business, one of the biggest potential threats to the business is the stability of this relationship and what happens if the relationship ends in divorce? This threat needs to be managed carefully in the family, because if the newly introduced family member feels continually isolated, this can increase family tensions and may actually increase the possibility of divorce.

This threat is heightened once the next generation is included in the ownership of the assets, as divorce can risk these assets being split. Legal structures and binding financial agreements can be arranged to manage the financial impact of divorce. Speak to a good accountant and lawyer to explore these options.

#### Protection from challenging the will

The wishes of the older generation expressed in a will can be contested by family members of the next generation if they feel aggrieved about the division of the family assets. In recent times, courts have tended to consider the equal division of the family assets as the solution, which may lead to the will being successfully contested. In this case, the family member who was going to continue with the family farming business may not be able to take on the added debt needed to pay out siblings which may result in the family farm being sold so that the assets can be divided.

One of the major strategies to manage against the risk of a contested will is to pass on the assets to the selected next generation before the will is enacted i.e. a 'living will'. With this strategy, the assets no longer reside with the older generation, so there are no assets to be contested. However, this strategy heightens the risk if divorce then occurs in the next generation.

The challenge for farming families is that you can protect the business from either of these risks, but it is very difficult to protect the business from both risks. If you are seeking answers in this area, speak with an accountant and lawyer who specialise in farming business and estate planning.

## 10.1.5 Meeting processes

There is no set structure to a succession planning process, as it should respond to the unique characteristics and needs of each family business. The succession planning process is conducted slightly differently by different companies that assist with helping farming families with succession planning. However, the following elements should be included in any succession planning process:

### Family involvement

There should be a series of meetings, the first of which is the most important. It is recommended that all members of the family be present at the first meeting, both those members involved in the farming business and those who are not.

It is at this meeting that each family member should be given a chance to contribute and have their wishes understood. Often the unspoken hopes and aims of the various parties vary widely and may even be mutually exclusive. Initially, the older generation should be allowed to put their wishes forward, which will form the foundation of the major aim of the succession planning process. Other family members should then be allowed to contribute.

While non-farming members may not benefit directly from the succession plan, it is important they both hear the views of others and be able to express their own views and wishes. This means they will hear these discussions directly from other members and not hear the information third hand, which may not be correctly communicated.

It is recommended that a number of family meetings be organised to develop the first draft of a succession plan. It may not be necessary for non-farming members to be present at subsequent meetings, if the major decisions have been made at the first meeting.

There may be general agreement about the objectives of the family succession plan. However, there may be issues that remain outstanding and require further research, such as eligibility for the Federal Government's aged pension, the taxation implications of land transfer and gifting, and the drawing up of wills. Tasks for further research should be allocated to various family members with further meetings scheduled where these findings can be reported and further refinements can be made to the succession plan. Considerable discussion may be needed to fully understand the needs and wishes of all family members.

Once the succession plan has been developed, it needs to be revisited on a regular basis to see if it is still the best plan and relevant as family circumstances may change. These meetings could be two to three years apart and should be predetermined so they are in all family members' diaries.

### Formal process

A formal meeting process is encouraged, incorporating the following elements: an agenda, minutes and formal agreements (such as a binding financial agreement).

An agenda is useful for any meeting, so that all the objectives are addressed and the meeting can be kept focused on the process and outcomes.

It is important that minutes be kept as a written record of all family meetings. These minutes should record major views, actions and resolutions as an important record for future reference, as the memory of all involved may not be reliable when recalling important information.

Separately written agreements should be made, especially if they are legal agreements such as 'binding financial agreements'. It is important that both formal and informal agreements be written and agreed to so that clear communication can be maintained.

### Independent chairperson

It is strongly recommended that an independent chairperson be used to ensure the meeting is conducted in a manner that encourages all to participate and prevents dominant family members from taking over the process. An effective independent chairman also means all family members can participate freely without having the responsibility of focusing on the process of the meeting.

A summary of the issues that need to be considered in order to work toward an effective succession planning process are provided in Table 10.1 (p. 206).

**'I farmed with my father for a few years. In subsequent years, my siblings came back, an older brother and an older sister. Over time, we'd been able to increase our land area from about 600ha to about 3500ha – we had a clearly defined goal to make three viable units. In 2008-09, we decided it was time to divide our business. That took about 18 months. It was done very carefully – we had a lot of independent help along the way to keep us on track because it's a very delicate process, as you can imagine! But we got through that process very well and as a result, I still talk to my brother and brother-in-law on a daily basis. We share machinery, we group finance together, so we've still got a lot of benefit from working together and we are in charge of our own destiny.'**

Michael Chilvers,  
'Winburn', Launceston, Tasmania

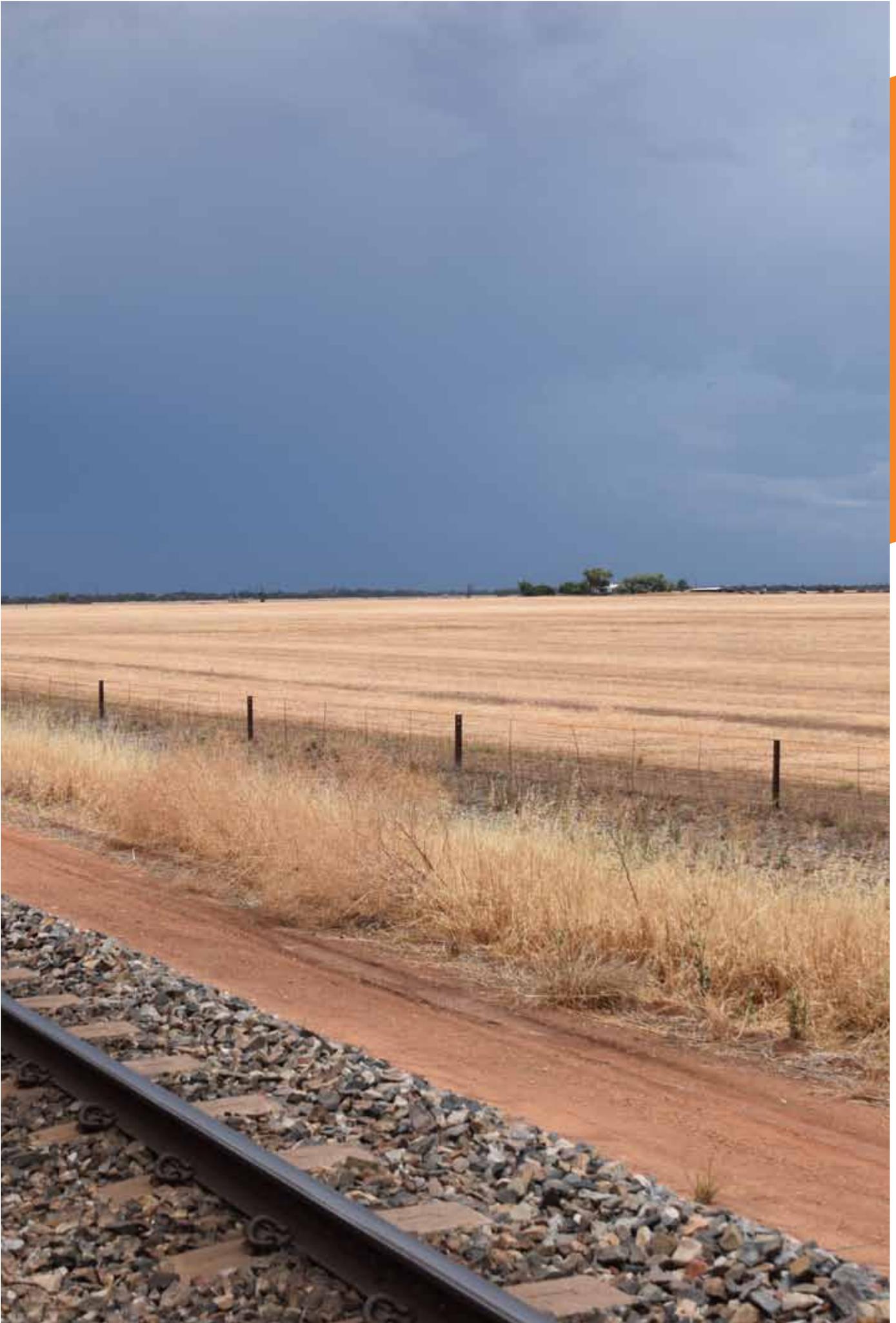


Table 10.1: Issues to consider and use as a checklist in your succession planning process

		Issues	Where are you in relation to this issue?	Comment
Timing	Proactive / reactive?	Do you plan well ahead or will you leave everything to be sorted out after your death?	<p>← Proactive: process planned years ahead.</p> <p>→ Reactive: No planning. Everything left until reading of will.</p>	<p>No plan may lead to problems:</p> <ul style="list-style-type: none"> <li>• Will is challenged.</li> <li>• Business and/or family relationships suffer. The proactive approach tends to result in more positive outcomes.</li> </ul>
	Inclusive / exclusive?	Is the process open and does it include everyone involved in the business?	<p>← All business decisions are transparent and the process is inclusive of everyone in the business.</p> <p>→ Business decisions and plans are not open to all, and exclude members, such as a new daughter-in-law.</p>	An approach that excludes certain members of the family/business may damage relationships and even impact negatively on the business.
People management	Rules of engagement	Is behaviour mutually respectful? Is everyone encouraged to speak freely and be listened to actively?	<p>← Each family member is involved and is given time to speak freely. All feel valued.</p> <p>→ Some family members feel de-valued by the process.</p>	If not managed well, this can put enormous stress on both business and personal relationships. Section 2, <b>Leadership and people management, Module 1</b> , may provide insight to this issue.
	Ultimate goal	To transfer farm to next generation? To exit farming as next generation do not want to farm? Other?	<p>← To transfer farm to next generation.</p> <p>→ Sell farm to meet retirement needs. Next generation to inherit what is left.</p>	See section 4, <b>Where is my business heading, Module 2</b> , to help with business analysis and goal planning.
Financial capacity	Farm business management	Will the farm have the financial capacity to meet needs of all family in the succession plan?	<p>← Whole farm analysis completed each year. Scenario analysis used to plan for future needs.</p> <p>→ No business or scenario analysis completed. Can older generation afford to retire or transfer farm to next generation?</p>	Measure business capacity to meet succession plans using financial 'tools' in section 5, How do I measure the financial performance of my farm business, Module 2. Test different management scenarios using section 11, <b>Analytical tools, Module 3</b> . Software can model possible scenarios for the business.

Issues		Where are you in relation to this issue?	Comment
Transfer of the business	Transfer of assets (Estate planning)	<p>How is estate planning done? Is it fair or equitable?</p> <p>Fair division: Farm secured as a viable, sustainable business. All family are happy with asset division.</p> <p>← Equitable division: regardless of impact on farm's viability. →</p>	NB. This is NOT the same as the transfer of management.
	Transfer of management	<p>When is management transferred at operational, tactical and strategic levels?</p> <p>← Younger generation given responsibilities early to develop experience in management. →</p> <p>Older generation will not let go and holds management control, particularly financial.</p>	NB. NOT the same as asset transfer. Section 4, <b>Where is my business heading? Module 2</b> , may help with planning management at all three levels: strategic, tactical and operational.
	Risk management	<p>Is farm protected from risks of:</p> <ul style="list-style-type: none"> <li>• divorce, death or disability.</li> <li>• the will being challenged?</li> </ul> <p>← Process in place to protect farm from these risks. →</p> <p>No protection in place. Will is challenged. Relationships and business may be threatened.</p>	Section 7, <b>Risk management, Module 3</b> , may provide further insight to this issue.
Meeting processes	Formal meeting process	<p>Are meetings effective? Are records kept and accessible to all?</p> <p>← All information and decisions are minuted and distributed. →</p> <p>Nothing in writing → confusion.</p>	Written records help minimise disagreements when memory fails.
	Independent chairperson	<p>Is an effective and independent chairperson used?</p> <p>← Independent chair. Meetings run efficiently and fairly, so all can be heard. →</p> <p>Chair is a family member. They, or another member, dominate meetings.</p>	An independent chair is critical to the success of an effective process. Meetings need to be run efficiently and fairly, so all can be heard.
	Family involvement	<p>Does everyone understand the decision-making process?</p> <p>← Decisions are made and enacted. All involved are satisfied with process. →</p> <p>Decisions are never made. High degree of emotional trauma and uncertainty about the future.</p>	If this process is procrastinated or ignored until a death or disaster occurs, outcomes are likely to be significantly less successful.

NB. This list is not exhaustive as each farm business and family is unique. This is provided as a guide only.

Source: P2PAgri P/L

## 10.2 HOW DO YOU START THE SUCCESSION PLANNING PROCESS?

The first step is to assess whether the older generation, regardless of their age, have a written succession plan. If they don't, then their willingness to begin the family succession planning process needs to be determined. These first two steps are needed before a viable succession planning process can start.

The choice of an independent chairperson is important: they need to have empathy with the process and be skilled in ensuring all family members present are able to participate and be heard. They also need to be trusted by all involved. If you do not have a person in mind for this role, you could research the following people:

- Ask neighbours who have gone through this process and see who they recommend.
- Ask your accountant for their recommendation, which gives them a chance to say they would be willing to facilitate a family meeting or they could recommend a professional who has worked with other clients.
- You could also ask your banker for their opinion, as they may know of other clients who have successfully gone through this process.

When you have compiled a short list, make a decision and approach that person. It is important to start the process; it is rarely seen as being urgent, often resulting in the process being procrastinated.

Once you have begun the process, use Table 10.1 (p. 206) as a checklist to determine issues that need to be addressed to suit your unique family and farm business situation.

David: 'Give the next generation the responsibility that they need, to come into the business in a management role sooner rather than later so that they know and are fully up to date, how to run the business before I want to step back, and not waiting until I take the exit ramp.'

Nell: 'He involves me a lot in making management decisions which I probably wouldn't get working somewhere else. I'm here at an operational level, but he does involve me in decision-making. I think there's huge potential in the industry and with the growing population of the world, there's always going to be a demand for food. Farming's becoming more and more efficient, using technology, skilled labour, and education's a very important thing for young people.'

David and Nell Mott,  
'Berryjerry Station', Wagga Wagga, NSW

### Action points

- If you do not have a workable family farming succession plan, start the process today.
- If you do have a succession plan and it hasn't been reviewed for 3 years, then have a family meeting and review the plan to see if adjustments need to be made.
- If you have successfully completed a succession plan pat yourself on the back for the good work as most family farms have not completed this process.
- Don't leave the succession plan to others to determine, which may happen if nothing is done!

