

Planning for the Farm/Ranch Business Transition

George W. Haynes, Ph.D.
Professor and Extension Specialist
Montana State University – Bozeman

Mission and Goals



Quality of Life - *Happiness*

- Personal
 - Good Physical and Mental Health
 - Good Financial (Economic) Health
 - and others
- Community
 - Healthy social environment (basic freedoms, minimum conflict, minimum corruption, etc.)
 - Security (no crime, no political upheaval)
 - and others

Who Cares?

- Successful **farmers/ranchers** develop mission statements and set goals?
 - E.g., debt retirement
- Successful **families** develop mission statements and set goals?
 - E.g., send children to college
- Successful **farm/ranch families** develop mission statements and set goals?
 - E.g., debt retirement *and* send children to college

Why -- Farmers/Ranchers?

- **Uncertainty**
 - Weather
 - Production uncertainty
 - Participate in world markets (for grain) and national market (for livestock)
 - Price uncertainty
 - Family events



Courtesy of the Billings Gazette

Mission Statement

- Developing a simple mission statement
 - Remember – the process is more important than the actual mission statement itself (involve everyone)
 - Try it!

GOALS

Process of Setting Goals

- Self-Assessment
 - The self-assessment recognizes agricultural production and family life interactions and focuses on interests, skills, motivations, and satisfactions for all members of the family and business unit.

Exercise

- Farming and Ranching Self-Assessment
 - Complete by yourself – take 5 minutes
 - Discuss

Farming and Ranching Self-Assessment

October 20, 2011

The questions ask you to identify sources of satisfaction and motivation related to: (1) dimensions of family life, and (2) dimensions of farming or ranching. For each source, there are three questions. If you cannot think of a question that doesn't apply to you, skip it and go on to the next. Check the box that most closely describes your response to each question. The abbreviations mean:

SA = strongly agree; A = agree; U = undecided; D = disagree; and SD = strongly disagree.

Questions	SA	A	U	D	SD
1. I'm glad my home is on a farm or ranch.					
2. When days I look forward to doing whatever is to be done.					
3. I'm satisfied with business working as my primary source of income.					
4. I enjoy the variety of challenges generated by life on a farm/ranch.					
5. I think living on a farm/ranch is the best living situation that I could have.					
6. I'm glad my work was better on a farm or ranch.					
7. I enjoy the office work (keeping records, paying bills, and other work) that is required in farming/ranching.					
8. I like to buy and sell livestock and/or livestock products.					
9. I like to buy and sell grains, hay, produce, and other products.					
10. I enjoy being able to keep costs down when purchasing or selling vehicles and equipment, or negotiating with lenders and dealers.					
11. I enjoy the business dealings required when purchasing or selling vehicles and equipment, or negotiating with lenders and dealers.					
12. I enjoy looking ahead, gathering information and making long-range management decisions.					
13. Compared to others in the community, I think we get better crop yields and/or higher production of livestock and livestock products.					
14. Compared to others with similar operations, I think our net income tends to be greater.					
15. Compared to others with similar operations, our debt level is less.					
16. Compared to others in the community, I believe I've worked more and managed better.					

+ 2 questions

Keys to Success

- Mission Statement
- Goals
- Objectives

TRANSITION



Stages of Succession

- Pre-business
- Education and personal development
- Proof of competence
- Formal start
- Declaration of succession

Longnecker, et al., 2008

Why Join the Family Business?

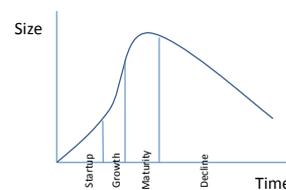
- **Desire**-based commitment
 - Deep-seated, gut-level attraction to the business
- **Obligation**-based commitment
 - Really ought to pursue a career in family business (birthright)
- **Cost**-based commitment
 - Too much to lose by doing something else
- **Need**-based commitment
 - Not sure I can succeed outside the family business

Longnecker, et al., 2008

Intergenerational Issues

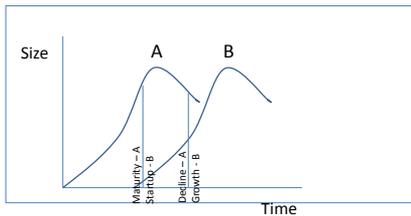
- Leaders typically serve long terms and tend to be risk adverse
- Business management information is not passed down to younger generation
- Successors reluctant to challenge predecessors' beliefs and ways
- Older generation does not want to let go; next generation may lack passion

Transitions



Business Life Cycle

(diversification, innovation, entrepreneurship)



Transition Considerations

- Does my child possess the temperament and ability necessary for business ownership/leadership?
- How can I motivate my child to take an interest in the business?
- What type of education/expertise are needed?

Transition Considerations

- What timetable should in employing and allowing my child to “take over” the operation?
- How can I avoid favoritism?
- How can I prevent a business relationship from destroying my parent-child relationship?

Favorable Conditions

- Sound, profitable business
- Stable, healthy family relationships
- Advance planning for leadership succession
- Positive family leadership
- Presentation of career opportunities without pressure
- Open communication on family business issues

Big Risks (5 D's)

- **Death**
 - Life insurance
- **Disability**
 - Income protection – disability insurance
- **Disaster**
 - Insurance, savings, non-farm investments
- **Divorce**
 - Marital property agreements
- **Disagreements**
 - Agreement on how to sever business relationship

Source: <http://pubs.ent.uct.edu/446/446-610/section1-managing-risk.pdf>

Farm Management Proficiency Test

TRANSITIONING MANAGEMENT

Transferring Management

- Decision-making authority
 - General manager
 - One party has final authority
 - When is authority transferred to the young person?
 - Equal voice
 - Equal voice in decision-making, but provision for final authority if disagreement
 - Vote by all parties
 - Vote weighted by size of capital contributions
 - One party given final authority
 - Outside arbitration

Source: <http://www.extension.ilstate.edu/publications/PM1474A.pdf>

Dividing Roles

- If everyone is responsible for everything, no one is responsible for anything
- You cannot delegate what you cannot define; delegation without definition is abdication.

Wittman, p. 85

Traditional Case

- Boss made the decisions and did the work
- Everyone else = hired labor
- Boss worked until death
- Survivors continued with the farm
- Senior heir assumed management role
- Cycle started all over again

Modern Farm/Ranch

- Bigger and more diversified
- More partners and owners working together
- Farming/ranching is more “high tech”
- Potential successors
 - Better educated
 - Insist on some role in management/ownership
 - No tolerance for “bosses”
 - Want delegation and empowerment
- Managers and owners often aren’t the same group

Wittman, p. 84

Attributes of Good Managers

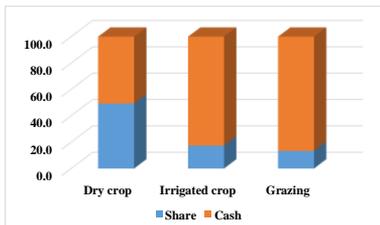
- Facilitator – not a boss
- Empowers people, doesn’t micro-manage them
- Focuses on people, resources, information, and technologies
- Promotes teamwork, positive thinking and professionalism
- Willing to be accountable to a “board of directors”

SUCCESSION, LEASING, OR SELLING

Option 1: Lease the place out

- Crop-share (or livestock-share)
- Cash rent
- Risk profile

Leasing Shares (cash & crop-share)



Rates

- Dry crop land
 - Average - \$26/acre
- Irrigated crop land
 - Average - \$78/acre
- Grazing land - \$21/AUM

Option 2: Transition to a Family Member

- Compensation (in near term)
- Inheritance (in long term)

Compensation & Inheritance

- Family member
 - Do you pay market rate for the help (manager)?
 - Do you pay “adjusted market rate” based on expectation to inherit the ranch?
- Challenge – are inheritance expectations fulfilled?

Option 3: Hire a manager (non-family)

- Compensation
- Communication
- Expectations (goals)

Compensation

- Ranch manager salary \$30,00 - ???
 - \$10/hr translates into \$20,800/year
- Benefits
 - Social security, unemployment, workers compensation
 - Health insurance (or funds to buy health insurance on the exchange)
 - Retirement benefits

Communication/Expectations

- Communications
 - How well do you and manager get along?
 - How durable (long-lasting) is the relationship?
- Expectations
 - Are net income expectations being met?
 - Are sustainability (stewardship) expectations being met?

Option 4: Sell it!

- Real estate commissions
- Basis
 - Estate taxation
- Investments
 - 1031 exchanges

Wrap-up and Evaluation