

Transferring the Family Farm

Family dynamics



In 2017 Statistics Canada published “A portrait of a 21st century agricultural operation” based on the 2016 Census of Agriculture. It sets out how farming in Canada has evolved over the years from both a human and operational perspective. The study finds that from 2011 to 2016, the number of farm operations in Canada fell almost 6% and the average age of Canadian farmers increased slightly to 55 years of age. On a positive note, the number of farmers under age 35 increased between 2011 and 2016, representing the first time there has been an increase in younger farmers in this age group since 1991. In addition, the number of female farmers continues to increase, with women making up almost 30% of all farm operators.

When it comes to the structure of farming businesses, a prominent trend identified in the report was the increasing use of farming corporations. Since 1971, farm operators have been moving away from sole proprietorships and partnerships towards farming corporations, which can offer certain business and legal advantages. Many of these agricultural operations are still operated by families, with nearly 23% reporting their operations as family corporations in 2016.

A key finding calls attention to using a written succession plan to transfer the ownership of an agricultural operation. It points out that in 2016, about 8% of all farm operators had a written succession plan, and about 16% of family and non-family corporations had a written succession plan, as compared with only 6% of sole proprietorships and partnerships.

A succession plan involves the transition of a farming business by the principal farm operator to the next generation. Alternatively, it may involve selling the business, or renting out farmland to a third party, while allowing the farm owner and his or her family members to enjoy the financial benefits arising from the sale or rental.

As with any family business succession plan, the earlier the planning begins, the better prepared the next generation may be to take over and continue the successful operation of the business. During the planning process, transition elements such as ownership, capital, management and labour will need to be discussed by the family as these elements can be closely tied to individual identities and roles within the family. Engaging in a constructive family discussion can often avoid family disputes and disharmony.

A farm succession plan should be distinguished from an estate plan. While a succession plan provides a roadmap for a transfer of business ownership to a successor, an estate plan provides for the distribution of accumulated wealth from an estate upon the death of a business owner. The latter will typically be given consideration within the succession planning process.

Succession Planning Steps

A typical succession plan involves the following steps:

- Start the conversation
- Gather and review financial information
- Discuss options and make initial decisions
- Develop the plan
- Execute the plan and monitor its progress

Start the conversation

As the bulk of a farming family's assets are frequently tied to buildings, land and equipment, the farm owner needs to have the assets properly valued to ensure that the succession plan works from a financial perspective so that everyone in the family may be adequately provided for. To deal with this issue, two key questions need to be addressed.

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First, is there one or more family members interested in (and competent to be) taking over the business? Second, how will the children who are not involved in the farming business be able to receive an equitable inheritance, if this is the desired goal?

As with many families, knowledge of financial planning may have been shared across generations in an *ad hoc* or incomplete manner. In this regard, professional advisors, for example, a financial advisor, lawyer, accountant and insurance specialist can fill the knowledge gap and provide their expertise in various aspects of the succession plan. They may also help with enhancing the flow of communication where emotions may affect sound decision-making and ensuring that the wishes and concerns of all family members are heard and addressed as the plan is developed and executed.

Gather and review financial information

The next step is to collect and analyze all the relevant financial information. It will be useful to compile tax returns, financial statements, banking information, financing arrangements, investment statements, as well as legal documents such as contracts, shareholder agreements and estate planning documents such as the farmer's Will and any Powers of Attorney.

In particular, financial statements are essential to analyzing the farm's past and current financial position and results of operations. They may form the basis for an appraisal of the farm's performance against industry standards and provide input into the process of business valuation, which is an important component in a succession plan. Cash-flow and earnings projections may provide a sense of the farm's viability and profitability, and help establish a value for the business that the farm owner may pass on to the next generation, or sell to a third party.

Discuss options and make initial decisions

During this stage, the farm owner and family members will identify issues, assess alternatives and make preliminary decisions. Some of the issues to be reviewed for purposes of the succession plan include:

- Identifying the successor and the method for the ownership transfer
- If the successor is a family member, are there any training needs, and should there be a period of overlap from one generation to the next?
- If there is no successor from the family and the farm is to be sold, how will the value of the farm be maximized for sale and allocated for estate distribution?
- Family living requirements: If the family is to be passed from one generation to the next, will the founding and successor generations occupy the farmhouse together? What will happen to non-farming family members? What are the monthly costs?
- Retirement planning needs of the farmer (and spouse)
- Business structure (sole proprietorship, partnership, corporation)
- Estate Planning issues (e.g., the impact of the farmer's Will and Powers of Attorney)
- Shareholders' or partnership agreements and dispute resolution mechanisms if the farm is transferred to more than one party

- Insurance needs
- Possible tenancy issues (leasing, various forms of tenancy)
- Financing options (family and external)

During the third step, the farmer and family members will assess "what if" scenarios that could come up due to disagreement, disability, divorce, natural disaster, and death.

This is the time to be realistic about any family tensions or differing goals among individual family members. For example, how could the estate distribution in a farmer's Will be affected if one child wishes to take over the farm, but two others children wish to move on and simply receive an equitable inheritance? What strategies might be used to equalize the inheritances of all the children? What is the farmer's timeline for retirement? How will the successor be trained to take over the farm? Will the retired farmer continue to contribute to the business by providing leadership or labour?

For further information that will assist you in tackling these questions, your TD advisor can provide other TD articles on issues involving business succession, estate planning, insurance and retirement planning. For specific tax management issues affecting family farm succession, ask your TD advisor for our companion piece to this article: *Transferring the Family Farm: Succession Planning Strategies*.

Develop the plan

Once the family has settled upon family and individual preferences and goals, the next step is to establish a written succession plan and to set a timeframe for the succession to take place.

The plan may include:

- An overall summary
- A business overview and financial plan
- A strategic plan to achieve family and individual goals
- A farm management plan

- A sale plan, if applicable
- A contingency plan, e.g., in the event of disability or premature death of the principal farm operator
- Supporting documentation

Execute the plan and monitor its progress

Once the succession plan is formulated and established, put it into action. Family members, professional advisors and relevant parties involved in the planning may require a copy of the plan. A timetable may be used to set out actions to be undertaken, and who is responsible for overseeing their implementation. Regular meetings can be held to monitor the progress and to address roadblocks which may arise and which may require alternate solutions.

Conclusion

Family farm succession involves a complex matrix of issues and takes time to execute. It is important to start as early as possible. When embarking on the planning process, consider engaging a team of professional advisors to assist in developing and implementing various aspects of the plan. This may include a financial advisor, business valuator, tax advisor, banker, insurance specialist and legal counsel.



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