

**PUTTING the FAMILY back into the FAMILY FARM.**

**OR**

**MODERN ESTATE PLANNING.**

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**ABSTRACT.**

**Provide children a business opportunity, as opposed to an inheritance.**

**The traditional estate planning attitude of handing on the family farm in to-days legal environment, to one or perhaps two members of the family, often places the future of the family farm, the mainstay of agricultural production in Australia, under threat.**

**Lawyers are actively encouraging parents to provide for their children equally or fairly and this has had a significant affect of passing on a viable family farm. The child who receives the family farm, now has to pay out their brothers and sisters their 'inheritance'. This in effect is 'buying the family farm each generation' and affects the potential for growth and use of new ideas and applicable research.**

**The average Australian family farm is valued around \$A 1 to 1 1/2 million and provides a significant asset base ( approx 89% equity) upon which to build or grow the family farm business – the Modern Estate Planning approach.**

**Changing the attitude from inheritance to growing the family farm business will provide opportunities for the children to develop a business perspective. This should result in an increased uptake of recommended research and ideas and provide a window of opportunity for agribusiness.**

Modern estate planning is the term I use to provide farm families a focus of building upon their family investment in their farm business, in order to provide opportunities for family members. This 'growth' perspective provides a contrast or alternative to the traditional inheritance approach of passing down the family farm, which in effect is 'breaking down' the family's significant investment between the children as they seek their inheritance 'share'.

The inheritance tradition, coupled with the annual production focus, makes the farm and not the family, the important aspect. This perhaps inhibits the farm family's ability to make necessary longer term changes and use appropriate agricultural research/technology to maintain or increase family farm viability.

The 'modern estate planning' focus is the result of many years of talking with and listening to farm family members comment on the ownership effects on both their family and their farm business. Many farm families have lost the family farm through the ownership situation, particularly where the ownership structure did not change with the changing family situation and the family had little or no understanding of ownership structures. Distrust between parents and their children on farm ownership issues generally results due to lack of understanding of ownership perspective's, by both parents and children, and the cost of gaining an understanding of ownership structures is seen to be prohibitive. Financial service providers have tended to be reactive, but at the same time many parents have resisted changes due to security aspects of what would happen if changes were to be made. Wills have also created problems for the farm family business.

### **Some major aspects that have significance for or impact on the farm family's ability to build or grow their family farm business for the future.**

#### **1. Buying the Family Farm each Generation.**

In today's legal environment, the child who inherits the family farm will generally be required to pay out brothers and sisters their share of inheritance. I have spoken to many farm families who inherited their family farm and have been paying out their brothers and sisters. They said the payments have restricted their farm business development and in some cases the level of farm maintenance required. There have been family situations where sibling payments have considerably reduced the family's ability to accommodate to significant market and climate fluctuations.

A year ago I was speaking with a farm wife, who is very proactive in the broader farming and farm family area, and she said that they had been looking forward to the completion of paying out brothers and sisters, only to be faced with increasing cash needs for their now teenage children.

This inheritance focus could well be a major inhibitor of the farm family's ability to make necessary changes or grow their farm business.

#### **2. The Family Farm is a Major Investment.**

During a 5 hour workshop on modern estate planning, I said the average Australian family farm was valued around \$1A to 1 1/2 million and that this was a very significant family investment. Participant comment was “-- have not looked at the farm like this before and whilst we know the farm value, we have not looked at it as a large investment, but rather as a production unit to be passed on, if a child wants to take the farm on”

Primary producers as a group are possibly the largest group of large investors in Australia and yet they focus on annual production. Focusing on the family investment to be built upon, allowing children to buy into the farm business is the modern estate planning approach and has been received with considerable interest by many farm families.

### **3. Understanding of Legal Ownership Structures.**

Feedback indicates a wide spread dependence on the farm families accountant to provide the appropriate legal ownership structure for the farm. Once the ownership structure has been set in place and the family feel comfortable with the structure, mostly partnerships, the structure becomes fixed. Should a family dispute arise later on, another problem arises where a family member seeks legal advise. Comment from a number of farm family members is that solicitor's will only represent that member and not assist with solving the family problem.

The ‘Forty Year Old Jackeroo’ is a significant issue, due to both a lack of understanding of legal ownership structures and a realisation of their significance over the family's lifetime. Many see ownership issues as secondary to farming with their parents, until later on the child finds themselves trapped, having worked a significant part of their life on the family farm, they have no asset. Worse is where their spouse has worked off farm and helped to subsidise the family farm. In many cases this child is told that they will get the farm in their parents will!

Capital gains tax has added a complication to the ownership issue, particularly with partnerships. Recently a spouse left a significant family farm partnership and her marriage. I mentioned the capital gains affects. This initiated an immediate reaction. Divorce can destroy the income earning capacity of other family members as well as the divorcing couple and this situation should be accommodated when setting up the ownership structure or making changes as the family members grow older.

### **4. Role of Farm Service Providers .**

The major farm service providers are specialists. The farmer is a generalist. Both focus on the annual production cycle or financial year.

Because the farm is the major or in many cases the only source of income for the farm family, the focus is the farm and the enterprises undertaken. The physical aspects of production being seen as paramount. This focus on the physical or production side of the farm has had far reaching effects, both for the farm family and the service providers, including agricultural education.

Agricultural courses tend to favor production with the financial and social sides seen as secondary. The majority of students excel at the physical agricultural side of courses and question why they really need to study the financial aspects, as they will not be involved in this area when they return home to the

family farm. Students are generally encouraged by staff to specialise, as this will aid their employment chances.

My first employment on completion of agricultural college was with the N.S.W. state government's Soil Conservation Service designing and constructing soil erosion control measures. I soon realised that contour banks reduced water runoff, but also reduced the filling of farm dams. Financial considerations were not considered. I was providing a specialised service.

Another example of the effects of specialisation from the farm family point of view. Young members of a multi million dollar farm business sought my assistance in regard to their family situation. Through the failure of one of their farm enterprises, they were in significant disagreement with the parents. Neither the parents or the children involved knew the financial situation, as this was handled by their accountant. I reviewed their taxation returns and found that the accountant was using a loan back scheme for the family trust for cash management purposes. However, the family were unaware of this and the tight financial position the family were experiencing was causing family friction. The family in effect had little control over their business and did not know what to ask the accountant. There was no business plan, but production ideas of what to do to return to a more viable position in several years time. I have also found the opposite position whereby the family had very good financial control of their business.

## **5. Policy Perspective's.**

The family farm business will continue to be the mainstream of the agricultural production sector into the foreseeable future. However, there is a need to provide greater focus on the farm family than previously and their overall ability to make or accommodate the changes that will be forced on them by the changing world food scene.

Ian Donges, President, National Farmers' Federation set out in the outline for his talk at the 'Country Matters' Conference, Canberra, May, 1999, the need to reinvent the clever country and that country people have always been innovative in facing up to challenges of our environment and place in the world.

There is no dispute that changes need to be made by country people, but to say that there is a need to reinvent the clever country tends to indicate that we have not looked previously at the agricultural environment as a whole.

Whilst there are driving forces for making changes there are also restraining forces of which I have mentioned some above. Actually there are mixed messages in the media.

The Weekly Times rural newspaper of 20th January, 1999, included an article titled 'Agri studies loses appeal'. The article said that agricultural courses were less popular and in fact had fallen some 25% during the past 3 years. Parents are saying to their children not to go into agriculture as income levels do not fair too well.

The agricultural research profession is well established, but the specialist research approach has actually reduced research use effectiveness. Researchers write for their peer group, as this is how they gain recognition in the research world.

The then Deputy Premier of Victoria, the Hon Pat McNamara when addressing a meeting of community and industry people in Horsham 9th April last year, said that when he took over the Agriculture Portfolio, he read the Annual Reports of the Research Stations. He found the reports very professional, but that is where the research stayed. He then suggested to his senior departmental staff that \$10,000 should be given directly to each farmer in Victoria to make up for the research-farming communication gap.

Extension officers have been the people directly involved with the farming community, but their training is in agriculture and is not sufficient to assist many farm families in broader family and ownership issues. A broader trained person is needed to augment the specialists. Government extension services have been, over the last few years, wound down in Australia.

Presently, the top 30% of primary producers produce around 70% of agricultural produce. There is a tremendous opportunity to assist with providing, at least a proportion of the other 70% of the primary producers, a chance of improving their farm businesses.

### **The Modern Estate Planning Approach - to put the family back into the family farm.**

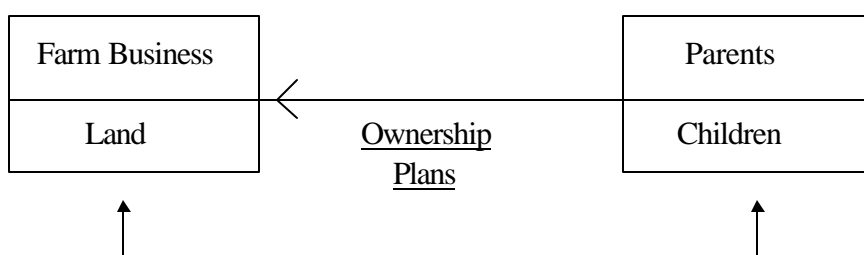
#### **1. The Relationship between the Family Farm and the Farm Family.**

The farm and farm family are generally seen as one unit. Therefore there is a need to separate the three major components and plan for each separately and then integrate the three areas to develop the overall whole farm family business strategy.

This separation is necessary, as there are two time frames involved. Concentrating on the present, the annual production, with little or no focus on the longer term is to increase risk of not achieving farm family goals. Equal attention to both annual and long term aspects is needed for overall risk management.

#### Family Farm Business

#### Farm Family



Business Plans  
(Series of 5 year plans)

Productivity increase to  
maintain business  
profitability.

**PLUS**

Family Plans  
(Series of 5 year plans)

Productivity increase to  
cover the increasing  
family cash needs.

## 2. Family Plans - the goals they wish to achieve and their cash needs .

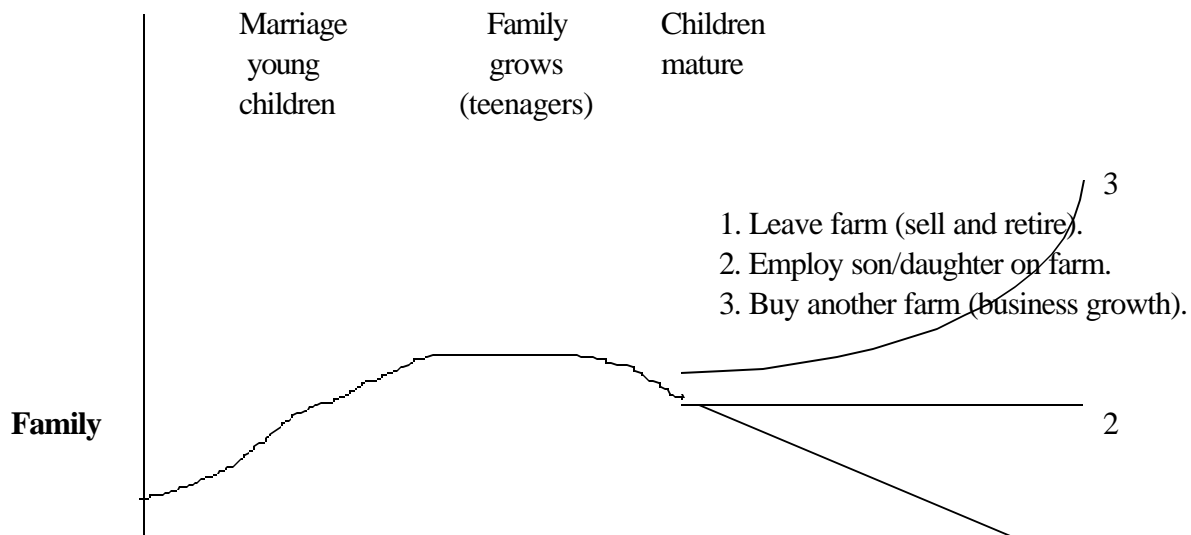
- a) Goals. Every family has a range of family goals, such as
- i) Providing their children better opportunities than they were provided.
  - ii) Keeping the family talking together.
  - iii) To treat each child as equally as possible and teach them life skills.
  - iv) For the farm business to be carried on. This also could provide for teaching children business skills as we are all taught by employees at school so where do we learn the business if not at home. Teaching all children business skills gives them an alternative to only being an employee.
  - v) Provide for an enjoyable retirement.

Family goals should be written down for the next five years for each of the above five goals, then resolve any conflict between the goals..

b) Family cash needs. These steadily grow as the family grows in both age and number. However, the annual cash produced by the farm is variable from year to year. As the family is the reason for farming , use of cash management techniques are paramount.

The family cash needs must be determined and then decide how the cash will be provided. Figure 1 shows increasing cash needs as the family grows. Budgeting for this year's farm income based on average of previous years production and cash income will very quickly pressure the family. Involving the eldest child in the farm business without growth of the farm business will put greater pressure on the family.

Figure 1. Individual's life cycle: life phases and cash needs



cash  
needs  
\$

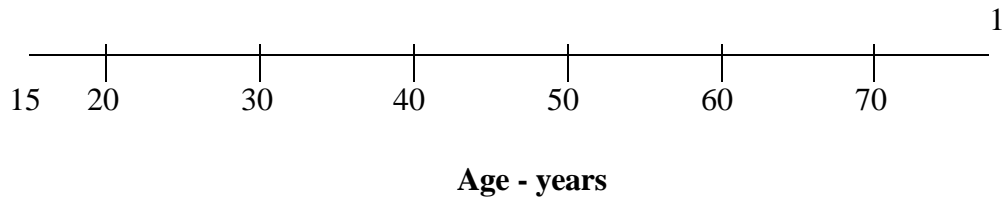


Figure 2:

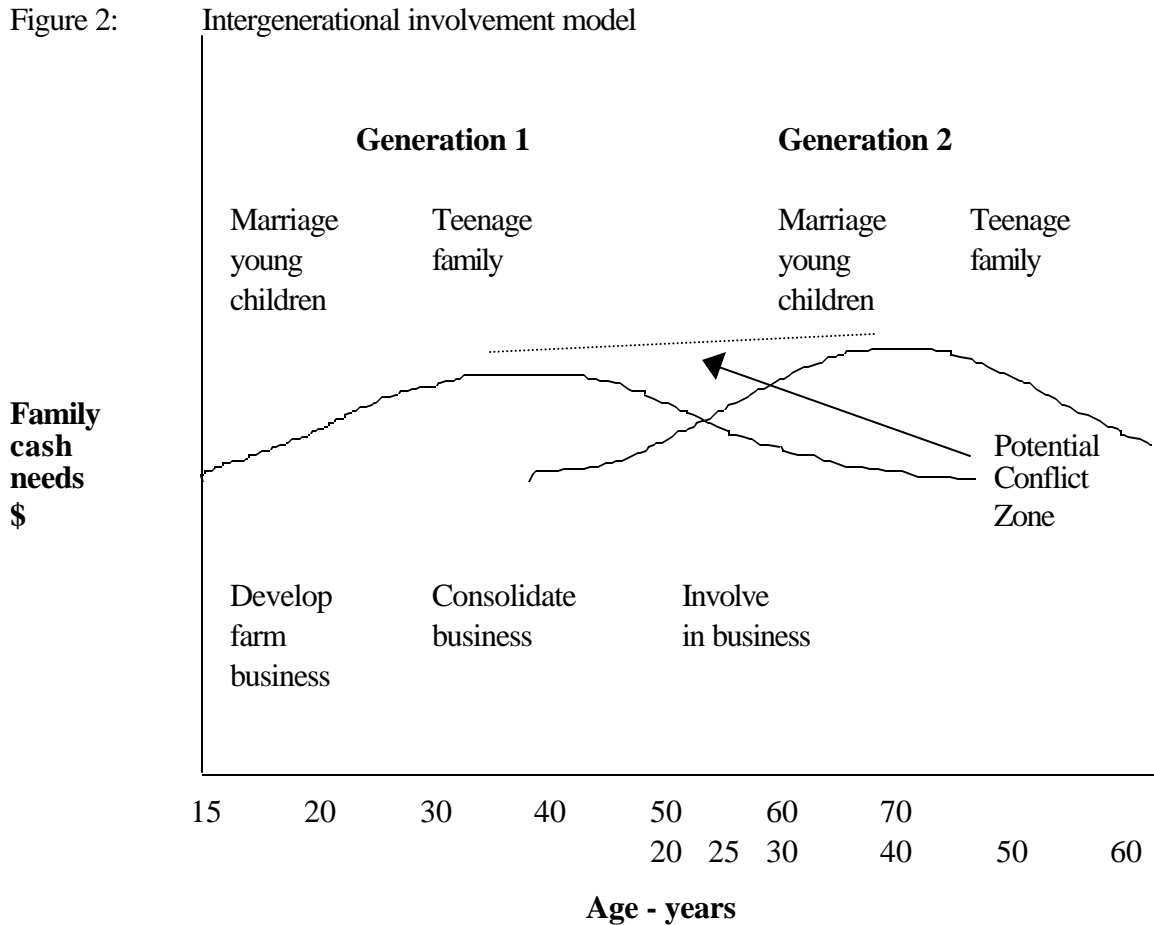


Figure 2 indicates the two cash needs positions and the potential for conflict between the two generations, e.g., the ‘forty year old jackeroo’ position.

**3. Ownership Plans - the key to growth and survival.**

a) Level of opportunity to involve children. The amount of cash available for the family will determine the opportunity base.

\$30,000 is the minimum cash needed for one family. For larger families and with private education, this amount quickly rises to \$60,000 and beyond.

\$50,000 is needed to involve 1 unmarried child working full time with parents in the family farm business.

\$30,000 is a 3% return on \$1 million

\$50,000 is a 5% return on \$1 million. These figures do not provide for tax payments or farm asset growth/maintenance. ( or paying out brothers/sisters their inheritance )

b) Type of involvement. Gifting of a family farm does little for the family inheriting and for the parents in providing for retirement.

A unit trust is the most flexible ownership structure and allows for children to buy into the family business. Another option I provide farm families is to split the land from the business and allow the children to buy into the business only. This provides for a greater business focus for the children. For a farm business to grow there must be an inflow of cash and buying in not only provides a source of cash, limited as it may be in the early stages, but provides the children a sense of earning their part of the business. Other situations are available, such as in a discretionary or fixed trust, a beneficiary can loan back a proportion of their distribution to the farm business.

A unit trust should also assist in preventing a divorce within the family from destroying the farm family business. The federal government has foreshadowed changes to the taxation of trusts which may reduce their popularity.

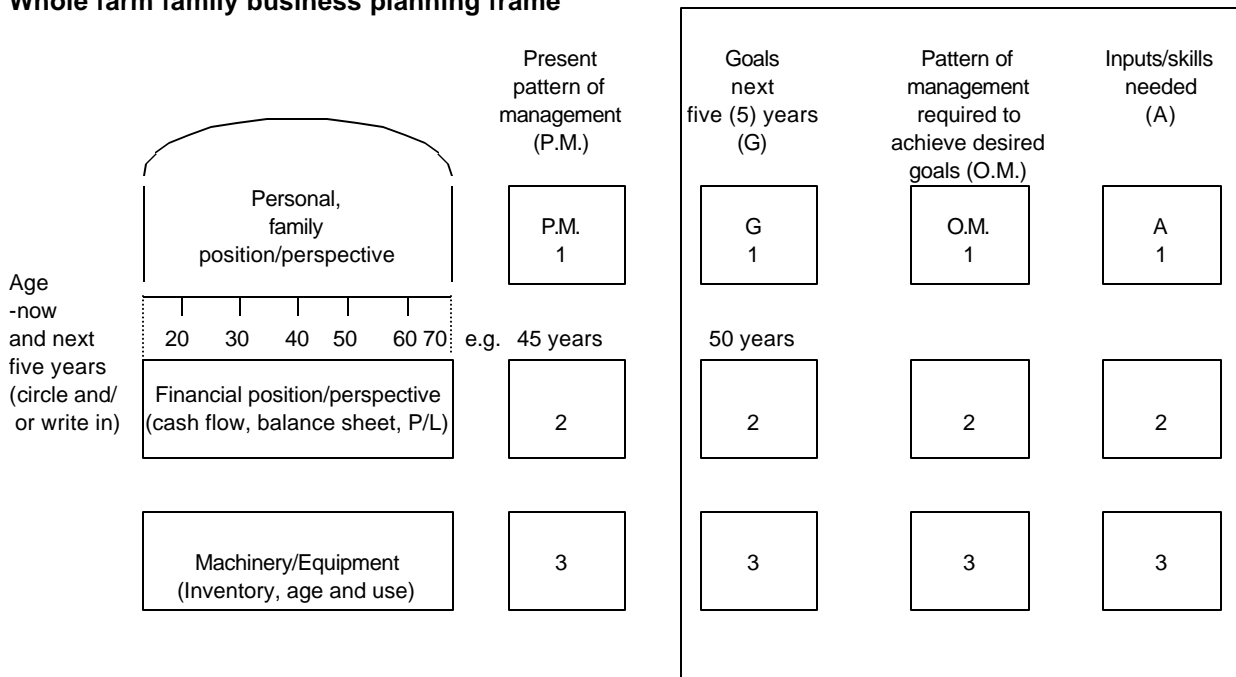
#### 4. Business Plans - how to achieve the family and business goals.

With any business you need to look at ALL aspects of the business. Concentrating on specific parts will not compensate for little, or in some cases, no attention to other parts of the business.

The following whole farm family business planning frame may assist with

- \* Looking at the relationships of the components of the farm business and placing into context, advice sought from specialist service providers.
- \* Developing a plan of how to involve family members in the farm business.
- \* Developing a business plan.
- \* Providing the basis for a family conference/regular discussion.

#### Whole farm family business planning frame



Livestock (Inventory and program)	4	4	4	4
Cropping, Pastures (Inventory and program)	5	5	5	5
Land soil type inventory and utilisation	6	6	6	6
Rainfall patterns and trends	7	7	7	7

This planning frame uses seven (7) very separate areas of an ON farm business. Not all areas are involved with every farm, e.g., a cropping farm would delete livestock or livestock could be left in should the business decide to diversify into livestock at a different location.

All areas of the planning frame **interact** and by working through the planning frame, weak areas are highlighted and needed advice and/or skills/resources sought.

Every component of the planning frame should be completed for the applicable area for where we are now, as this shows the relationships within the farm business. Ownership would fit in with the financial position. Goals for each of the applicable areas are next to be written down. Detailed goals then provide the basis for developing 5 year budgets and prevent knee jerk reactions to suggestions from others. Any suggestions should be considered, but in the light of the detailed plans. The fourth area of the planning frame provides what resources, skills or changes are needed to achieve your goals. Plans must be written down so that all in the family have access. Considerable time and effort is needed to develop necessary farm family business plans and these are necessary for two very good reasons; the value of the very significant investment in the farm business, valued on average around \$1 million and to keep harmony within and provide opportunities for the family. Family farm businesses are **BIG FAMILY INVESTMENTS** and should not be looked at as small businesses.

Business plans are not yet popular in Australia. Monash University recently carried out a national survey of farm family use of strategic business planning. The researcher found that 26% of the 748 respondents kept formally written business plans. However, 54% of these developed the business plans as they were required by the lending institution.

Modern estate planning is about considerably widening opportunities for the farm family through looking at the farm family and their family farm from a **comprehensive** point of view. A

comprehensive Manual is available that includes the issues discussed in this paper. This manual doubles as the study guide for an elective subject in the nationally available TAFE home study Rural Business Management course.

The family farm on average is a significant investment upon which to build. To increase the viability of the farm family business will have flow on effects for the greater rural community and the nation as a whole, including focus on the environmental effects of family farms improved viability in catchment areas.

To assist the farm family, I believe there is a need to provide for a broader trained generalist, who is recognised as just as important to the agricultural scene as the specialist providers. The farm family must also be recognised and not just how to increase farm physical productivity. To ignore these two areas is to give credence to the 'science of muddling through'.

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