

THE GPS SUCCESSION GUIDE

THREE KEY ISSUES EVERY FARM SUCCESSION STRATEGY MUST SOLVE

BY READING THIS REPORT YOU WILL:

- Know the real issues that break up family farms. (Hint... it's not estate taxes or probate.)
- Be challenged to look at farm succession from a different vantage point.
- Discover the road map that creates a cash flowable path to ownership for the farming heirs, treats the non-farming heirs fairly/equitably, and gives parents the peace of mind knowing their farm succession goals will be achieved.

WHY IS FARM SUCCESSION IMPORTANT TO YOU?

Parents spend a lifetime building a farm that started generations before them. It's their number one goal to keep it together. Yet, many have not taken the steps necessary to accomplish this goal. Hope is not a strategy, and an elimination of the estate tax does not solve the problem of family dynamics, cash flow, equitable farm valuation, or management control.

Farm succession has grown to be a hot topic over the years. Many traditional finance companies have attempted to jump into this space. The media continues to focus on the political football surrounding the ever-changing federal estate tax limit. To be fair, managing your estate to minimize losses is always important. No one wants the IRS to take money off the family table. However, estate taxes and probate are not the main cause for breaking up most family farms. The family is. Rather, it's the lack of a coordinated plan to manage the unmet or unrealistic expectations within the family that breaks up our farms.

It's the lack of a coordinated plan to manage the unmet or unrealistic expectations within the family that breaks up our farms.

If you want to successfully keep the farm AND the peace in the family, then you must plan by design, not by default. The estate documents that got you where you are today will not get you where you want to be in the future. Successful families design their strategies to solve three key issues to grow their operation each generation. The three main issues are:

- 1) **The Farming Heir's Long-Term Viability**
- 2) **The Off-Farm Heir's Independence**
- 3) **The Parents Peace of Mind**

If the estate documents do not include any provisions for the farm succession then the off-farm heirs have complete independence, but the farming heir could lose the farm and the parents' goals of keeping the farm and the family together are lost. On the other hand, if the farm is locked up so no one can get out, the farm will stay together but the family relationships could be lost. To accomplish the goals, we must design the succession strategy through the vantage point from all three critical players: the farming heirs, the off-farm children, and the parents. Let's look at all three.



THE FARM HEIR'S CHALLENGES

- It takes a larger land base to support a family today. Yet the default distribution from estate breaks farms into smaller pieces.
- The farming heir effectively pays for the farm 3 times: 1st as rent payments during the parents' retirement, 2nd as principal payments for the buyout, and 3rd as interest payments on the loan.
- Current cash flow off the farm cannot support major land purchases from the parents' estate.

1) The Farming Heir's Viability – The Coming Cash Flow Crisis

Is it fair to say that the number of acres it takes to support a family has grown over the last 10-20 years? Why is it then that most families make their farm smaller every generation? Think about it. The default action in the parents' estate documents is to give all assets to the spouse first, then split them equally between all the children, right? So instead of focusing on how to multiply the operation most families are dividing the farms into smaller and smaller pieces. How is that going to work if you are the one farming? Let's look at some of key challenges facing the next generation of farmers.

The Farm Heir's Math...

Let's take a family of six. Mom and Dad raised four great kids; one farming child and three off-farm children. They've grown their farm to 800 acres where the average land price is \$10,000 per acre and the average rent in the county is \$250/acre. What would it take for the farming child to buy-out the off-farm heirs if he or she wanted or needed to? The total land value is \$8,000,000 and to buy out 75% (the off-farm heirs' portion) the farming child would need to come up with \$6,000,000. Most young farmers do not have that kind of cash laying around. (Nor do too many older farmers!) If it was financed on a traditional 20 year note at 5.5% interest the total land payment would be \$502,075.98 (Principal + Interest) per year. That works out to \$836.80 per acre for the 600 acres purchased. How will that possibly cash flow when they were paying \$250 per acre in rent the year before? The land values may be different in your area, but the principles remain the same.

If we assume normal life expectancies and the estate is distributed when the heirs are in their 50's or 60's, how old will they be by the time the land is paid off? This poses significant challenges for the farming heir. Keep in mind that this does not include any buyout consideration for machinery, grain storage, or livestock facilities yet. Would you ever commit 20 – 30 years of farming if this was what the exit plan looked like?

The Farm Heir's Equity...

The section above made assumptions about bank financing. The simple truth though is that the loan might not even happen. Here's why. Most major ag lenders adjust the amount of financing based on the serviceability of that note. For example, they might allow you to buy land at \$10,000/acre but they will only finance \$5,900/acre because their underwriting suggests that this is the maximum amount of debt that the land income can support. In other words you need almost 40% equity up front just to qualify for the loan. This could be a challenge if there are three kids or more in the family! The farm heir may need to collateralize their own balance sheet just to keep the parents' farm whole.

Most farming kids grew up hearing about the time long ago when Grandpa and Grandma had to buy out their siblings. Then they watched Mom and Dad do the same. How many times can a family farm be split up and then made whole again? How many times should a family go into debt between generations on the same piece of dirt? It's exciting to use financing to buy a new farm, but it's tough to grow if you are using it to keep what is already there. It's also tough to confidently bid on new ground when you don't know where you stand on the family ground.

How many times should a family go into debt between generations on the same piece of dirt?

THE FARM HEIR'S CHALLENGES

- How old will the farm heir be by the time the buyout from the estate is paid off?
- The business relationship with the parents is fundamentally different than with the siblings, in-laws, nieces and nephews.
- It's difficult for the farming heir to make long term plans for the operation and his or her own family if they don't know the parent's plan for the farm distribution.



Please do not misread this. We are not critical of banks. In fact, it's just the opposite. Bank financing is a crucial part for expanding the operation. Here's the issue. Which farmer is more likely to get good financing? The one who inherited 25% of a family farm with no succession strategy? Or the farmer looking to expand because they own 100% of the family farm as designed by their succession strategy?

Perhaps you feel like you do not need a farm succession strategy for your family. But understand that someday you will need to compete against the families that do. Farms have need to grow in order to stay competitive. We cannot continue to think about how our farms can make it to the next generation. We need to think about how we can grow through the next generation.

Perhaps you feel like you do not need a farm succession strategy for your family. But understand that someday you will need to compete against the families that do.

The Farm Heir's Control...

Perhaps one of the most rewarding aspects of being a farmer is that you get to call your own shots. You may not always call it right, but at least you know who to point the finger at when things don't work out. It's not management by committee. Sure, there is often a team involved in key decisions but they are all working towards the same goal. You can respond quickly based on what you see in the markets, your agronomy, your tax situation, etc.

How does the operational management look after the land is distributed to the kids? Does a majority vote win? Improvements are often necessary in the operation. Perhaps it's tiling, terracing, or fertility. Buildings need to be built, repaired, or torn down. Who makes that call? To the farming heir it's an opportunity to add long term value (and maybe some tax write off's) to the operation. To the off-farm heir this is an expense that comes off of cash flow. Will their goals be aligned?

What if one sibling is not happy with the rent income? Maybe there's a big operator in the area that is paying top dollar for rent. Is there anything that says the ground must be rented within the family? Maybe the siblings all get along okay and none of this is an issue. But what happens if one of the siblings pass away? Will the surviving spouse (or nieces and nephews) see things the same way? Farming has always offered a rich environment of uncontrollable events. You can get hailed-out a week before harvest. The balance sheet can swing by hundreds of thousands of dollars after a bad week in the market. A disagreement in management decisions does not have to be one of the uncontrollable events. The right farm succession strategy can provide consistency regardless of who owns the land.

THE OFF-FARM HEIR'S CHALLENGES

- Many states have partition laws which lead to a sale of the property if it cannot be effectively divided when someone wants/needs out.
- Will the 2nd or 3rd generation of off-farm heirs share the sentimental appreciation of the farm as the 1st generation?
- Their only way to capture any gains in land value is to sell the farm.

2) The Off-farm Heir's Independence – Are They Feeling Stuck?

Everyone knows of at least one family where the kids couldn't get along and the farm that the parents and grandparents spent lifetimes to build up was quickly sold out. Everyone is in a raw state of mind when a parent passes away. There is a mental shift that occurs. Some people have a hard time thinking long-term after just experiencing the shortness of life.

Sometimes the survivors put on a strong front because they know "it's what Mom and Dad would have wanted". They may even suggest that they will come back to help out along the way. Then over time the sentimentality of the family farm legacy starts to wane. The demands and pressures of everyday life start to creep in. Friction within the family and the farm can occur slowly at first, then suddenly. Once one child sells, it often creates a domino effect. It's hard to collect a small rent check after they watch a sibling cash in their chips for a large pay off. But wait... land has traditionally been thought of as a good investment, right? It's a source of income. Why would anyone ever sell?

Once one child sells, it often creates a domino effect. It's hard to collect a small rent check after they watch a sibling cash in their chips for a large pay off.

The Off-Farm Heir's Math...

What would you define as a good investment? What kind of return would you expect? Is the investment locked up? Or is it liquid? Let's go back to the previous example. The four children inherited 800 acres valued at \$10,000 per acre. The average rent for the county was \$250 per acre. Let's say that the average property tax for owning farmland in that county worked out to \$25 per acre. This means that the net income is \$225 per acre (\$250 rent per acre minus \$25 property tax per acre). If you divide the net income by the actual land value on a per acre basis you get $\$225 \div \$10,000 = 2.25\%$ rate of return on the land asset. Would that 2.25% meet your expectations of a good return from the start of the paragraph? To be fair, this only represents the rate of return for the income. The land will go up (or down) in value too. The capital appreciation should be included as part of the return. However, how does one ever realize the actual capital gain on land? They must sell it. If they sell it, then this puts the farming heir back into a negative cash flow position. The seller's gain is the farm heir's pain! As farmers we do understand the value of land. But how would you view the 2.25% ROI ("Return On Inheritance") if you were the off-farm heir? Would it be the highest and best use of capital for your family?

The Off-Farm Heir's Equity...

Inheriting land can significantly boost the financial net worth of the heirs. Some see this as a humbling experience where the fruits of Mom and Dad's labor is realized. Others see their bump in net worth and it gets their motor running on all the things they can do with it (both positive and negative). How does the off-farm heir ever realize the equity from their inheritance? The farming child can always collateralize the land to expand the operation. Every year the off-farm heir watches their sibling purchase new equipment, build barns, or take on new ground to grow the operation or minimize taxes. Yet when it comes time to distribute the rent in March and September it seems like the cash flow is ironically tight. "How can this be?" they wonder. The farming sibling can use their credit line to run their business however they see fit. Can the off-farm heir collateralize their share as well? As the parent or the farming child, would you really want them to collateralize the land base for their own needs? Probably not. Inheriting land significantly boosts the financial net worth for all children. The question is, what can they really do with it in its present form?

THE OFF-FARM HEIR'S CHALLENGES

- The income rate of return is often perceived as low when compared to alternative options or paying off their own debt.
- If the value comes from the rent, then almost all of their inheritance ultimately depends on the performance of their farming sibling.
- It's difficult for the off-farm heir to utilize the equity in their inheritance without jeopardizing the farm operation.
- Off-farm heirs can feel stuck between the farming sibling and the financial pressures, goals, and opportunities within their own situation.



The Off-Farm Heir's Control...

Human nature is funny. We may love to build sand castles. Maybe we could create moats and bridges all day long on a wide open beach. But what happens when we are told that we don't get a sand beach. We get a sand box. In that box is a very specific set of sand toys and those toys have to be shared with others who are also confined to the box. Now, even though we love the sand and we may even like the others playing in the box, it doesn't take long for someone to get a little sand in their shorts. Getting thrust into a farm business with other family members and in-laws can kind of feel the same way.

The best businesses are run by owners that choose to come together because they share a common goal, have complimentary skill sets, and can provide sweat equity and/or capital to get the business going. The key here is that they "choose" to come together. They are not forced into a business relationship. How much control does the off-farm heir really have in the operation? What if they wanted to use their inheritance to fund their own goals or their own business? Is that wrong?

In most circumstances the off-farm heir is not trying to cause a problem with their farming brother or sister. But every night they have to go home to their spouse, their kids, and their financial demands. They have to make the best decisions for their situation too. This unintentionally puts them in a rather tight spot.

In most circumstances the off-farm heir is not trying to cause a problem with their farming brother or sister. But every night they go home to their spouse, their kids, and their financial demands.

It's possible that the ideal landlord is the off-farm sibling who just sits quiet, collects a rent check, never needs a cash infusion, and is just happy with the added income. Many would point out that any inheritance is a gift regardless if someone is farming or not. That is tough to argue. The simple truth however is that we live in a dynamic world with competing ideas and demands for resources. It might be difficult to maintain business and family relationships in this environment. Especially if the off-farm heirs see their situation as owning an illiquid asset that provides a low rate of return.

When the farm heir's options are limited the control mechanism of choice is typically to ratchet up the rent or sell the land. These unmet expectations can be resolved through an effective farm succession strategy so if someone wants out it doesn't break up the farm. It is possible when the best strategies are implemented and adequately communicated between the farming and off-farm heirs.

THE PARENTS' CHALLENGES

- It's easy to feel overwhelmed by all the noise surrounding farm succession.
- Determining "fair" vs. "equal" can be impossible if there is no model to work from.
- It's hard to know what to do when you don't know the options and you don't know who to trust.
- Transition is inevitable. If you decide not to decide, then you just made your decision.

3) The Parent's View – Well Intentioned Diffusion

It doesn't matter who we meet or what part of the country we are in, most parents' goals fall into four main categories:

- They want to protect the farming heir's interests.
- They want to treat the off-farm heirs fairly/equitably.
- They would like to live comfortably with peace of mind in their decisions.
- They don't want to lose anything to Uncle Sam.

An effective farm continuation strategy will go deeper into each category until the parents' intentions are fully refined. Which interests need to be protected for the farming heir? How would that be defined? How long are those interests protected before the farming heir needs to act on his or her own? Do we base "fair" on today's values or does it float with the overall market? How does the family really determine "fair" versus "equal"? Are we talking about equal asset value between the kids? Is it equal income potential regardless of the asset class? Or do they mean that each child has an equal opportunity to use their inheritance to pursue their own goals? What is it going to take for the parents to live comfortably? How much cash flow is needed? What does it look like for them as the farming heir takes on more of the operation?

How does the family really determine "fair" versus "equal"?

Goals without actions are merely wishes...

It's easy for analysis paralysis to sink in when both the challenges and the options are overwhelming. It makes it hard to move forward with your goals. How do you know what to do if you don't know what the options are? Yet decisions do have to be made if the farm is going to successfully pass on to the kids and grandkids. Otherwise the farming heirs grow frustrated knowing that their operation could be at risk and the off-farm heirs wish they would "just do something" so they don't have to hash it out after the parents are gone.

We have come across many families where the parents basically decided to "punt" the ball because they couldn't come up with the right game plan. "We'll just let the kids figure it out" they say. Or they become passive on their decisions because "all their kids will get along". Yet when asked if they ever wished that they could go back and share ownership, control, and profit with their own siblings again we get a resounding "Heck no!" How is it that we wish upon our kids something that we would never wish for ourselves?

It's a little crazy. We spend our entire lives raising our kids to be fully independent. We tell them they can be anything they want to be if they work hard enough. We encourage them to discover their unique gifts and pursue their own path. The discipline that worked on the oldest child probably didn't have the same effect on the youngest. The amount of support one child benefited from might not have been needed by the others. Our principles remain the same for all our kids but the tactics we use to prepare and motivate them gets optimized based on their unique situation. Yet what is the default strategy that is used to distribute most estates? We treat the kids as if there is absolutely no difference among a single one of them! The land is divided equally. The machinery is divided equally. The grain inventory, bank accounts, brokerage accounts, ethanol/biodiesel stocks all divided equally as if each child benefited from all asset classes the same. This is typically done under the pretense of being "fair". Does this make sense?

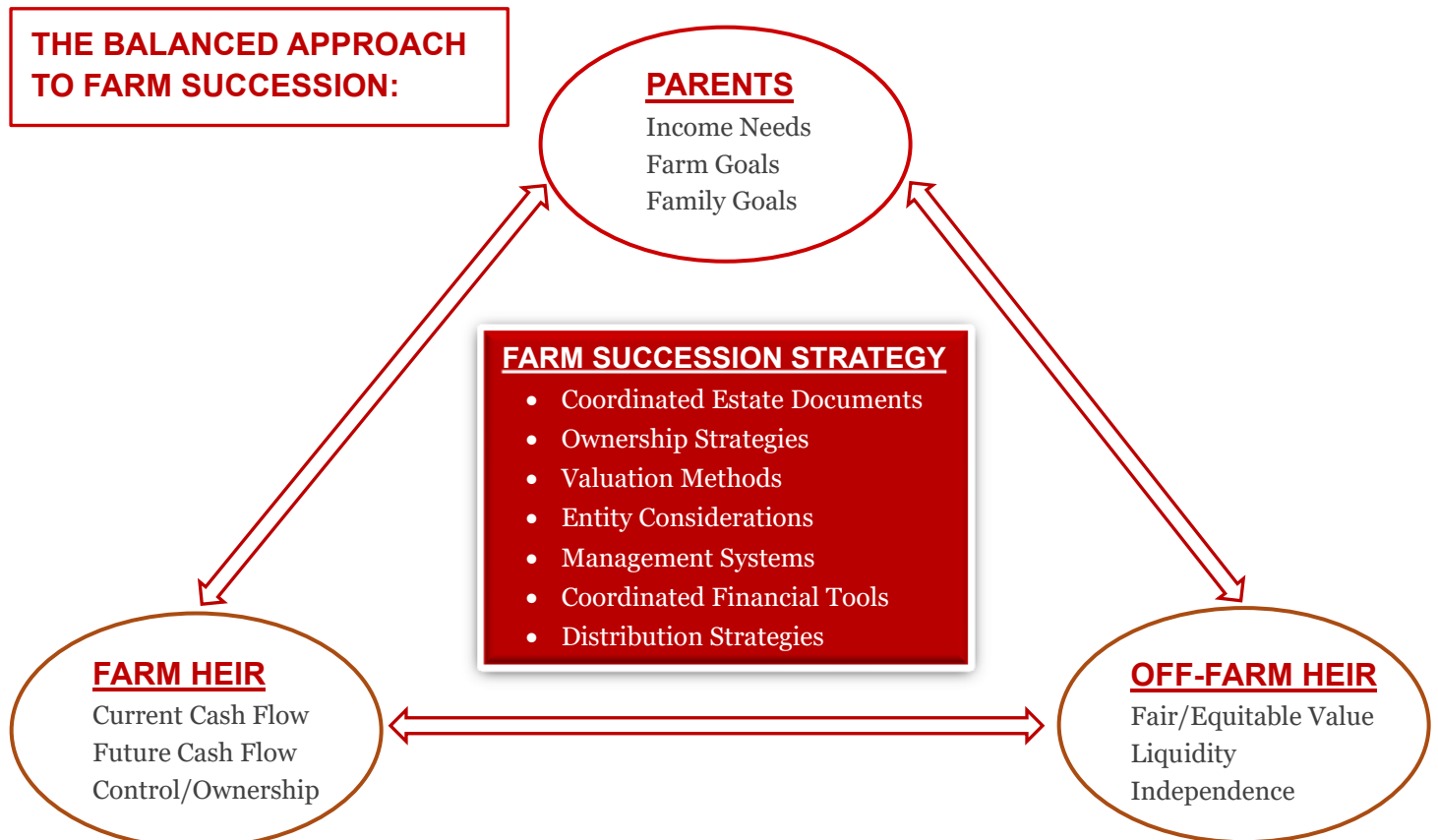
What if we approached our estate distribution with the same intentionality of how we raised our kids and grew our business? Such action would benefit everyone in the family equally. The challenge for most parents is that they are not sure where to begin, what options are available, or who to trust. Therefore nothing gets done. Sometimes they feel like they are stuck in the position of being the referee between the farming and off-farm children. They want to help the kids, but they also face challenges of their retirement needs. Will their farm income be enough? Can it support long term care? How long should they stay active on the farm?

The challenge for most parents is that they are not sure where to begin, what options are available, or even who to trust.

Parents, it is not your fault that the current ag cycle makes cash flow tight right now. It's not your fault that the kids have different priorities regarding their inheritance. It's not your fault that it takes time to map out the succession of the business and lifestyle you spent the last 30 or 40 years creating. It's not your fault that we must revisit this when the tax law changes. None of this is your fault... but it is your problem. You are uniquely equipped to solve this problem seeing as how it is your estate to manage, they are your kid and grandkids, and your children will most likely listen to you before listening to each other. There is a process to work through this. You just need to take the first step.

PUTTING IT ALL TOGETHER

Farm succession strategies fall apart when they fail to address the unmet or unrealistic expectations of the family members. It's the balanced approach that can keep it all together. The strategy must balance the goals for the parents, the farming heirs, and the off-farm heirs to the fullest extent possible.



OUR APPROACH

- Create great information, that's accessible to farm families to help them understand and solve their farm succession problems.
- Identify the families farm succession goals.
- Develop valuation methods within the family's goals.
- Integrate the most effective farm succession tools .
- Coordinate ownership, entity formation, and financial tools where needed.
- Work with our clients existing advisors so all are on the same page.
- We have three levels of service to help guide you to make the best decisions regardless of where you are in your journey.



The 3 Points of a Balanced Succession Strategy

Each point in the triangle represents a key component of the farm succession strategy. All points must be satisfied if both the farm and the family are to stay together.

The parents could charge embarrassing low rent so the farm heir can save up cash for the eventual buyout. The off-farm heirs would still get their full value from the estate, but the parents don't spend their lives building their business just to go out in a financial whimper to please the kids. Plus, how many years would it take to save up enough for the buy out?

The parents could just give the farm away to the farming heir. It would certainly cash flow for the farm heir today and in the future. If they gave the farm away today though the parents lose their income source. If they gave the farm to just the farming heir through their estate then the off-farm heirs feel cheated and the holidays probably won't be celebrated the same way as in the past.

The parents could just keep pushing off the planning. They continue to get their income along the way. It cash flows for the farming heir today, but not in the future unless a solid plan is in place.

Our Approach

It takes a balanced approach to determine the valuation and distribution method for farm land, machinery, and operational entities. Each asset class has its own implications. We look at all of the best practices for farm succession and match the distribution for each asset with the available tools depending on the individual operation and family goals. We also consider options for entity structures and financial tools that will accelerate the transfer and funding goals. We want to find the most efficient and cost-effective way to get each family member in the position they want to be. We also work with our clients existing attorneys and advisors to make sure that each legal document compliments the family's overall farm succession strategies.

WHERE DOES YOUR JOURNEY GO FROM HERE?

Would you like to learn more about the farm succession strategies that work without traveling to countless seminars, feeling like you are just being sold a product, or getting overwhelmed by all the "noise" in farm succession?

Whether you are just trying learn more, need help designing your own customized farm estate plan, or are looking for ways to optimize an existing plan, we have the tools to help. We have three online membership levels designed to meet you where you are today and help guide you to where you want to be, in the most efficient way forward.

Our Farm Estate GPS SEED, GROW, and HARVEST Memberships will equip you to make the best decisions for your farm and your family all at a pace that works for you.



Farm Estate GPS
Generational Planning Strategies

Your Online Guide to Farm Succession

GPS Membership Levels

Designed to meet you where you are with your farm succession planning and help get you to where you want to be.



SEED Membership

Helpful tips and notifications of events & training through Farm Estate GPS.

- ✓ Free Download: "GPS Succession Guide: Three Key Issues Every Farm Succession Strategy Must Solve"
- ✓ Email notices for blog updates
- ✓ Insight on farm succession issues
- ✓ Webinar access
- ✓ Helpful tips for estate and farm succession strategies
- ✓ Definitions of key terms
- ✓ Email notices for GPS events and training opportunities

FREE

[JOIN ONLINE](#)



GROW Membership

Tools, concepts, and strategies to help you make the best decisions for your situation.

- ✓ All SEED Membership features
 - ✓ Expanding library of video modules
 - ✓ Key definitions & farm estate FAQ's
 - ✓ Emailed articles
 - ✓ Video and Print Topics Include:
 - Cash flow and equity limitations
 - Farm vs off-farm heir perspectives
 - Defining "Fair" vs "Equal"
 - Family dynamics
 - Valuation methods
 - Sources for estate losses
 - Wills and trusts
 - Ownership and gifting strategies
 - Entity strategies
 - Financial tools to fit the plan
 - Management control
- Plus many more!

\$250/Year

[PREVIEW VIDEOS ONLINE](#)

[JOIN ONLINE](#)



HARVEST Membership

One-on-one support to design & implement your customized farm succession strategy.

- ✓ All GROW Membership features
- ✓ One-On-One Consulting
- ✓ Goal Development
- ✓ Estate Strategies
- ✓ Farm Succession Strategies
- ✓ Coordination of Financial Tools and Asset Ownership
- ✓ Collaboration with your legal and tax team
- ✓ Videos & Resources for Ongoing Support

\$2/Acre

\$500 Min / \$2,000 Max

\$250/Year HARVEST Renewal

[APPLY ONLINE](#)

Simply log on to start your journey today!

www.FarmEstateGPS.com



Farm Estate GPS

Generational Planning Strategies

www.FarmEstateGPS.com

YOUR COMPLETE GUIDE TO FARM SUCCESSION AT YOUR FINGERTIPS AND AT YOUR OWN PACE

- Understand the challenges and solutions to farm succession.
- Discover the tools and concepts that fit your farm best.
- Make informed decisions for the future of your family farm.
- Full 24/7 access to fit your schedule without pressure or stress.

Contact Us

Farm Estate GPS, LLC

2029 400th St.

Osage, IA 50461

Phone: (641) 732-3636

Email: fieldservice@farmestategps.com

Copyright © 2018, Farm Estate GPS, LLC. All right reserved.

Farm Estate GPS, LLC does not provide legal advice. The information we are providing is general and educational in nature and should not be considered legal or tax advice. Laws and regulations are complex and subject to change, which can materially impact your estate plan. Consult an attorney or tax professional regarding your specific situation.