Farm and business succession: Staging over time

The purpose of the article is to set out the "nuts and bolts" of staging succession to allow time to deal with and manage competing factors.

As with all farm and business successions there are several competing factors that need to be balanced, including;

- Income and financial security for the parents;
- Affordability of buying for succeeding child or children;
- Financial risk of parents still being involved in the farm/business e.g. parental guarantee to bank;
- Relationship property claims on farm assets from succeeding child's spouse;
- Handover of control both practically and legally;
- Alignment of Wills and memorandum of wishes with the succession plan e.g. the goodness of debt;

Below is a table that sets out an example of a staged process that addresses these key issues.

#	Stage	Action	Legal steps
1	Child returns from overseas (mid to late twenties)	Works on farm under manager and/or parents	Employment contract
2	Child wishes to buy into farm	Purchases half share in stock & plant in partnership with parents	Partnership agreement, simple sale and purchase agreement of stock and plant, lease of farm to partnership
3	Child wishes to get married and take over farming operation. Parents wish to step back from operation	Child buys out partnership and establishes own company/partnership with spouse to own stock & plant	Agreement to buy stock & plant, partnership wound up, new company/partnership established, lease from parents' trust to child's company/partnership
4	Parents wish to retire from farm	Child buys out freehold (or part of) with own trust. Child borrows to do this. Capital is used for parent's retirement	Child establishes new trust, sale and purchase of land at valuation, borrowing plus vendor finance from parents' trust and/or parents trust retains share
5	Survivor of parent dies	Outstanding loans/debts are forgiven on death. Remaining share of farm (if any) is transferred to child	Will and/or trust provides for forgiveness of debt. Parents' trust distributes remaining share of freehold as per directions in memorandum of wishes

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No one size fits all but the above stages or variations can be used in most scenarios. The key is allowing the successor to buy into the business over time with the price being affordable but the purchase price also allowing the parents to receive sufficient capital to assist in their retirement. There is also the need to free up capital for non-farming children. A staged approach also allows parents to receive income initially as partners and later as landlord throughout the trust;

In terms of relationship property claims a spouse or partner's claim can only relate to property held by the successor child and as such if the farm is in a separate parent trust, then it is unlikely to form part of relationship property. However, a parental trust is not a " silver bullet " and the child's interests, rights or powers relating to the trust, as well as the history and administration of the structure, will be relevant and may make the trust vulnerable to claims. Ideally, the trust is supported by a contracting out agreement, but these are not always practical to achieve.

In addition, to trusts, debt is also a useful instrument in limiting the relationship property risk. A relationship property claim can only relate to the equity in the asset after debt, whether that is the bank or parental vendor finance. The debt will need to be properly documented.

A staged process also allows for control to be handed over over time with the successor child being in partnership with Mum and Dad prior to taking over the farming assets and the relationship continuing after that through the lease of the farm from the parents' trust;

Lastly, it is important to ensure alignment of parents' wills and memorandum of wishes to ensure that the remaining debt is gifted off and allowances made for the non-farming children. Early on, there may need to be an acknowledgement that it may not be possible to achieve an entirely equal treatment of the off-farm children to achieve an affordable farm succession. Sometimes this is possible as the parents may have significant off farm assets e.g. Mum's inheritance, but this is often not the case.

The expectations of all parties need to be managed in relation to value and timing.

Want to know more?

If you have any questions, please contact our specialist Rural and agribusiness team.

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