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Farming for Generations: An investigation into the challenges of farm businesses remaining in the ownership of the same family for several generations

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Abstract

The three main aims of farming for succession are providing adequate funds for retirement, providing a viable farm for the next generation and providing a fair share of family wealth to all family members, including those who are not involved in farming. Achieving successful succession is difficult and takes a long time. Farm families need to start building the business early in life, work hard, consistently perform well, keep the family engaged, have a plan and maintain open and honest communication between all family members. Consistency of purpose is the key. Planning for succession, farming well and grasping opportunities that emerge are necessary to achieve the size of farm operation at which succession is a feasible choice. Scale is important, but scale alone will not enable the achievement of the three main aims. To enable the achievement of all the three main aims the older generation has to be prepared to let go, the younger generation has to be prepared to take over and the whole family has to be satisfied with the result. It is never too early to start planning for succession.

This paper provides the key insights and findings arising from a significant doctoral research study that was designed to explore this central concern across Australian farms.

Keywords: farm family goals, managing farm succession, farm business growth, farm planning

Introduction

Farming businesses are complex businesses to manage. The biological systems of soil, plants and water and the interaction between them are only partly under the control of the individual farmer and the markets into which the farm production is sold are volatile and outside of farmer control. The complexity increases when the business is a mixed enterprise, typically livestock and crop. Further increases in complexity occur if the business is family owned and operated, and the level of complexity is lifted again if the family aims, and attempts, to keep the farm in the ownership of the family. There is a further level of complexity if a proposed change in ownership is from siblings to cousins.

This study was about family farms in Australia that are used for growing crops, running beef cattle and sheep, or operating with a mix of these activities. These farms are classified as broad-acre farms. The majority of Australian broad-acre farm businesses are family owned, yet few families retain ownership of a farm business for several generations. Some owners of broad-acre farms plan to take their assets out of farming by selling the farm to fund retirement and also to pass on capital freed from farming to offspring to use outside of agriculture. The study has little relevance for those farmers.

The focus of this research (Stephens, 2020) was intergenerational succession of family farm businesses in the context in which there are three main aims (Wright and Kaine*,* 1997) of owners of family farm businesses. The definition of the three main aims is:

- To provide adequately for retirement;
- To pass on to heirs a farm that has reasonable prospects of being a sound economic proposition and financially viable and has potential for future improvements in productivity and growth of wealth for the farming child or children; and
- To provide a share of resources for the non–farming children that they consider as being adequately commensurate with their entitlement and with which they are content.

The evidence is that achieving the three main aims is not an option for most farm businesses, primarily because they lack sufficient scale.

Motivation for the Study

The theorist about the growth of the firm, Penrose (1995), wrote about the critical importance of 'the innards' of the firm in growth of the firm. She found that:

'Many firms do not grow and for a variety of reasons: un-enterprising direction, inefficient management, insufficient capital raising ability, lack of ability to adapt to changing circumstances, poor judgement leading to frequent and costly mistakes, or simply bad luck due to circumstances beyond their control. I am not concerned with such firms, for I am only concerned with the process of growth.' (p.7)

'History' is likely an important factor in succession. Owners of farm businesses that remain in the hands of one family for several generations generally develop a sense of history and have useful corporate memory. In relation to history, Penrose (1995) wrote: 'One of the primary assumptions of the growth of firms is that "history matters"; growth is essentially an evolutionary process and based on cumulative growth of collective knowledge*'* (p. xiii).

The present research was as concerned with why businesses did not continue as it is with why they did. The major case studies and historical records investigated in this study point to the important differences in skill, attitude and commitment to achieving the three main aims.

The majority of farm businesses in Australia make insufficient profit, too irregularly, to have a long-term, multi-generational future. In Table 1 is shown the distribution of the 50,000 broad-acre farm businesses in Australia by value of sales for the 2018-19 financial year.

It is unlikely that a farm business with a current total value of annual sales of $400,000 or less will be able to withstand the future vagaries of markets and climate and achieve the three main aims of farm owners aspiring to succession. If a broad-acre business currently had a gross value of annual sales of over $400,000, the business may have the growth potential to bring the three main aims within reach. The implication is that approximately one third of broad-acre farms businesses, or between 16,000 and 17,000 (Table 1) of them, have a size measured by annual gross value of sales sufficient to achieve the three main aims of providing adequate funds for retirement, providing a viable farm for the next generation and providing a fair share of family wealth to all family members, including those who are not involved in farming.

Unless (i) the older generation is prepared to hand over the business to the next generation, (ii) a member of the next generation is prepared to take over the business, and (iii) the needs, wants and aspirations of the non-farmers (in the next generation) are satisfied, the three main aims cannot be achieved. For many, the choice between a viable farm for the farming child and an equal or near-equal or fair distribution to all the children is too difficult, so they do nothing. If there is an intent to continue the business into the next generation, scale alone will not ensure that the three main aims will be achieved.

Table 1. Distribution of broadacre farm businesses by value of sales (total cash receipts), 2018-19

Sales class	Number of farm businesses	Share of population	Cumulative share of population	Share of value of sales	Cumulative value of sales
	no.	%	%	%	%
Less than $70 000	8,870	18	17.7	1	1.4
$70 000 to $120 000	6,900	14	31.4	2	3.8
$120 000 to $170 000	4,750	9	40.8	2	6.3
$170 000 to $230 000	3,740	7	48.3	3	9.0
$230 000 to $300 000	4,480	9	57.2	4	13.2
$300 000 to $400 000	3,540	7	64.3	4	17.7
$400 000 to $500 000	3,130	6	70.5	5	22.7
$500 000 to $620 000	2,920	6	76.3	6	28.6
$620 000 to $760 000	2,220	4	80.7	5	34.0
$760 000 to $900 000	2,010	4	84.7	6	40.1
$900 000 to $1.1 million	1,330	3	87.3	5	45.0
$1.1 to $1.3 million	1,230	2	89.8	5	50.3
$1.3 to $1.6 million	1,350	3	92.5	7	57.3
$1.6 to $1.9 million	890	2	94.2	6	62.9
$1.9 to $2.5 million	1,210	2	96.6	10	72.5
$2.5 to $3.1 million	560	1	97.8	6	78.0
$3.1 to $4.0 million	470	1	98.7	6	83.7
$4.0 to $5.0 million	300	1	99.3	5	88.6
$5.0 to $7.0 million	190	0	99.7	4	92.6
$7.0 to $10.0 million	120	0	99.9	4	96.1
Greater than $10.0 million	0	0	100.0	4	100.0
Total population of broadacre farms	**50,260**				
Total value of gross sales $ billions in 2018-19 $	**33.6**				

Source: Australian Agricultural and Grazing Industries Survey (AAGIS). *Note*: AAGIS excludes farms with an estimated value of agricultural operations of less than $40 000

The Study

The research question posed was: What abilities, attitudes, actions and strategies enable farm businesses and farm families to: (i) achieve the aims of providing adequately for retirement of the current farming generation; (ii) hand on a farm business that is an economically efficient and financially sound operation with sound prospects for increasing productivity and building further wealth; and (iii) provide fairly for all relevant family members.

A secondary research objective was to develop a model to allow real-time succession planning. The model was developed and used in the Succession Analysis and Planning (SAP) case studies.

Four research propositions were investigated:
(i) Survival of a farm business for several generations will not happen by chance.
(ii) Despite differences between non-farm and farm firms, theory about the growth of businesses generally, or their failure to grow, applies to farm firms, as do some practical determinants of the growth of, or failure to grow, of non-farm firms.
(iii) Not all farming families want to achieve the three main aims.
(iv) Farm size and performance are necessary but not sufficient conditions for intergenerational survival of farm businesses. A determination to grow the business to enable choices is a necessary prerequisite of achieving the three main aims.

To understand why so few farm businesses achieve the three main aims, in this study a mix of research methods were used. A pilot survey through an advisor network provided an assessment of over 6,000 of the 50,000 broad-acre family farms in Australia. Surveys of farmers and agricultural professionals and case studies of the farm succession experiences of families were documented.

Following the collection of information from 6,000 Australian broad-acre businesses, 16 case study businesses were analysed in detail and the historical records of 100 case study businesses were explored and their stories of succession documented.

The case study method was used to analyse and contrast attributes, attitudes and actions of family businesses; half of these 16 family businesses will continue farming, the other half will not. Characteristics of farm businesses whose owners have achieved successful succession for several generations, and ways this has been achieved, were contrasted with farm businesses whose owners have not achieved this goal.

Central to the question of farm succession are the attitudes and attributes, experiences and actions of the owner-managers who run farm businesses. The final line of inquiry was to conduct succession analysis and planning studies for five real-life, current family farm operations facing up to the question of succession. The real situations of farm owners, family members and managers, who have been through, or will go through, succession, were investigated. To do this, a method was developed and implemented which involved defining alternative future succession scenarios for the farm family, and determining the circumstances of farm production, profit and annual productivity growth, resulting in accumulation of wealth, that would need to apply over the planning period for the aspirations of the succession plan to be fulfilled. The financial model at the centre of the succession planning method was built on the assumption that accumulated wealth is from the reinvestment of earnings as well as nominal and real capital gain.

The attributes and attitudes and skills of the family members and the market and climatic environment in which the family operates led to the questions about size of business used in the financial model.

Answering the size questions is a fundamental step toward the three main aims. The research components and processes involved are shown in Figure 1.

Findings: How the three main aims were - or were not - achieved

Families in which the three main aims were achieved were committed to long term planning. Much research indicates that a farm family can achieve succession only if the business is sufficiently large (measured as capital base and annual gross value of farm product). This research indicates that, most commonly, a larger-scale business was actively sought by the owners because of a determination by the family to grow the business to create choices from wealth, including succession choices. The evidence from the research inquiries supports the proposition that farm business succession is only likely to be achieved successfully where there is significant asset growth over each generation. But, growth alone is not sufficient to ensure succession will be achieved. In many of the case study businesses in which the three main aims were achieved, the succession plan was not commenced or implemented until the children in the next generation were young adults. However, to make this possible, the parents had started planning for succession when or before the first child was conceived. They planned early for the possibility of succession but had no defined succession plan until later when more was known about the aspirations of their offspring.

In addition to a vision and determination to grow the business, families who achieved succession successfully demonstrated and delivered leadership and dedication to the business and a plan. The plan was supported by consistent hard work, a team approach, intelligent leadership and high-level business and farm management skills. The critical business skills included a sound understanding of managing risk and employing capital – their own and that of others. Farm management skills, regardless of the enterprise or enterprise mix, were used to consistently achieve high-level performance.

In the study most of those families in which the three aims were achieved had a long history of successful succession and had started to involve the next generation in the business at an early age. History matters. Conversely, in many of those families where the primary motivation was to run the current operation sufficiently well to achieve immediate aims, such as meeting debt-servicing commitments, and without explicit ambition to increase the size of the business over time and as opportunity dictated, the business became unviable and/or the family no longer owned it.

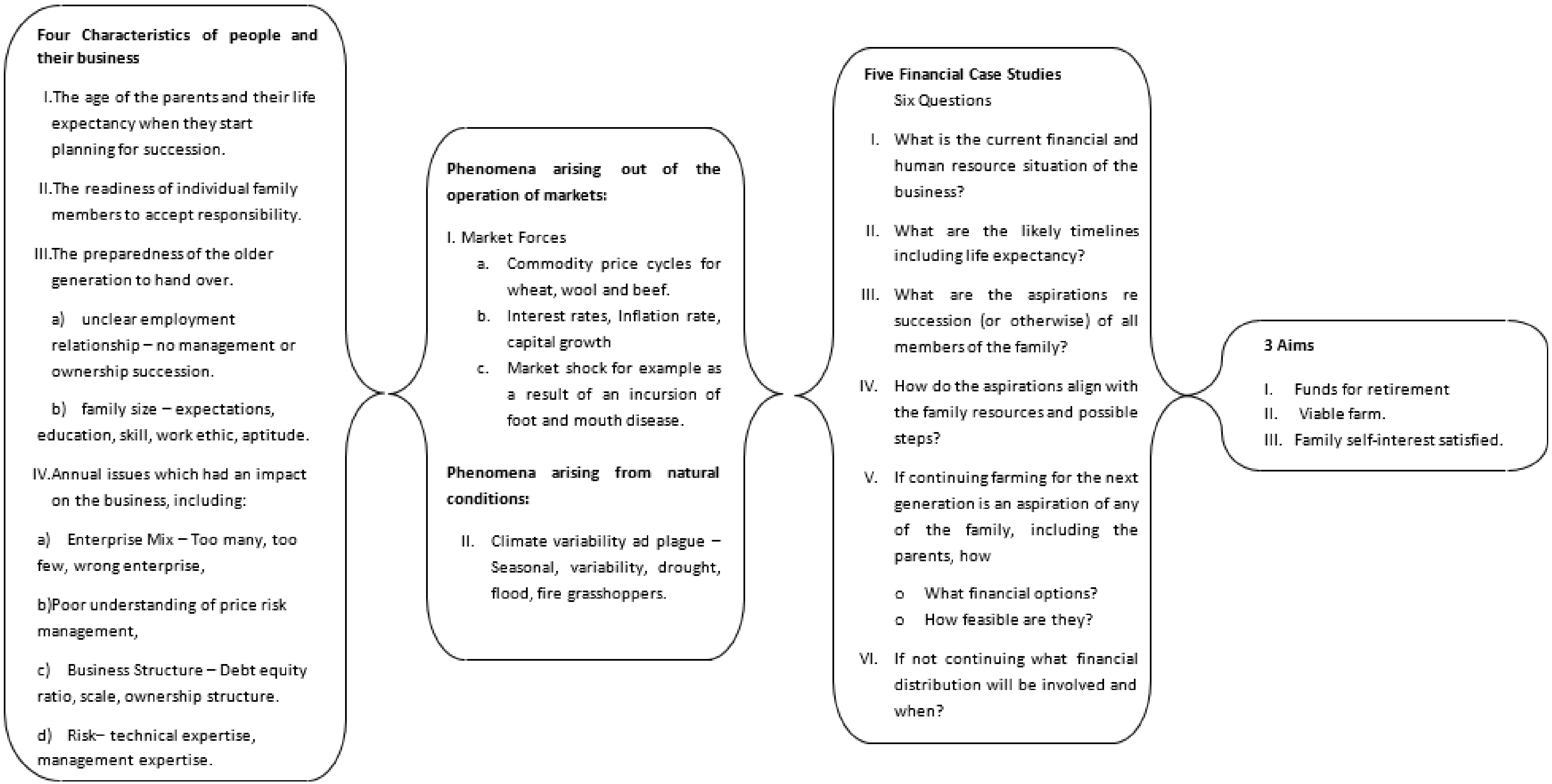
In the 100 business cases extracted from the historical records, 22 per cent of them were able to achieve the three main aims, but only 11 per cent of them were able to achieve the three main aims *and* achieve an equal distribution.

From the survey covering 12 per cent of the 50,000 broad-acre farm businesses, it was indicated that most of the owners of broad-acre family farm businesses who were surveyed did not have a succession plan, did not intend to develop a succession plan for their business and did not currently have the size of business and total equity to achieve the three main aims. It seemed that farm owners faced with the choice of putting the interests of the farm business above the interests of the non-farmer family members, or vice versa, found the decision too difficult and did nothing about future succession.

Of the 116 farm businesses that were studied in depth, 30 intended to continue beyond the third generation and were well-placed to do so. Of the 30 farm businesses that will continue into the next generation:

- 100 per cent have handed control to the next generation at a young age.
- 93 per cent set growth goals to enable succession.

Figure 1. Family, Environment, Questions, Three Main Aims



- 91 per cent ran higher than average stocking rates.
- 88 per cent built size and equity through a staged approach, increased livestock numbers, leased land and purchased land.
- 73 per cent had a history of smooth succession.
- 68 per cent had families where siblings worked together to grow and then split the business.
- 68 per cent worked for off-farm income.
- 68 per cent established a new 'on-farm' business.
- 67 per cent traded land.
- 64 per cent received periodic, significant injections of family capital.
- 48 per cent share-farmed extra land.

The final question investigated was about a practical way to 'do the sums' to inform participants in the succession process about what is at stake in the process and what is potentially possible. The essential features of the method of analysing prospects for successful succession under various plausible scenarios that was developed is shown in Table 2. The performance of the current farm business with the current farm plan is defined for the most common seasonal and market conditions, and likely performance extrapolated over the planning period involved. For decision-making about succession, the interested parties are trying to answer the following questions.

i. What is the current state and potential of the farm business? This question involves the whole farm approach of considering all of the main human, technical, economic, financial, risk and beyond-the-farm-gate elements that make up the farm business.
ii. What are the likely timings of key events in the future; both events over which there is choice and events that are inevitable such as life expectancy[1]?
iii. What are the aspirations for succession (or otherwise) of members of the family?
iv. How do these aspirations align with the family resources and possible future levels of these resources?
v. If continuing farming for the next generation is an aspiration of any of the family, including the parents:
    - What financial options exist?
    - How feasible are they?
vi. If not continuing the farm business, what financial distribution will be involved and when?

The forecast increase in net worth at three levels of business performance is shown in Figure 2. The highest level is aspirational and unlikely to be achieved. The mid- level is realistically achievable. The lowest level would almost certainly result in the business failing unless the manager took some intervention to avoid such failure.

The aim of modelling the future situation is to establish an agreed set of reasonable estimates about the 'family equity' that will be available for use and distribution through the succession process. These sums form the basis of defining alternatives and negotiation amongst all parties with an interest in the succession in question. Individuals involved will have unique situations, goals, aspirations and requirements and rates of time preference for present consumption versus future consumption, for control over their own share eventually. Each individual will apply their own set of preferences to the agreed set of numbers.

[1] The Australian Institute of Health and Welfare (2018) statistics indicate that on average women have a life expectancy of 85 and men of 81. These figures have been used in all the financial case studies.

Further, to put things into the current perspective, the members of the family will want to know the likely future values of assets, debt and equity in terms of current dollar values? Converting future values to current equivalent values helps to form, and inform, views about what assets might be able to be procured in the future with the future value of equity, if the values of current assets expressed in present value terms are a reasonable guide to their future value. These future and present values of assets to be shared in succession plans are calculated below for each case study and shown in tabular form (see Table 3).

Table 2. Future situation #1 (2.1% operating return on capital + 4.2% nominal increase in land value)

Representative		Description	Current situation current $	Future situation future $	Future situation current $
Real return on assets	4%				
Inflation	3%	Values from the balance sheet			
Market rate of interest	7.12%	Land assets	$ 7,000,000		
Time period	30	Stock	$ 2,700,000		
% Nominal operating return	2.1%	Plant	$ 300,000		
% Real increase in land value	4.2%	Other	$ -		
		Liabilities	$ 3,000,000		
		Net assets or equity	$ 7,000,000	$62,513,822	$25,754,867
			Rounded	$ 60,000,000	$ 26,000,000

Figure 2. Forecast increase in net worth

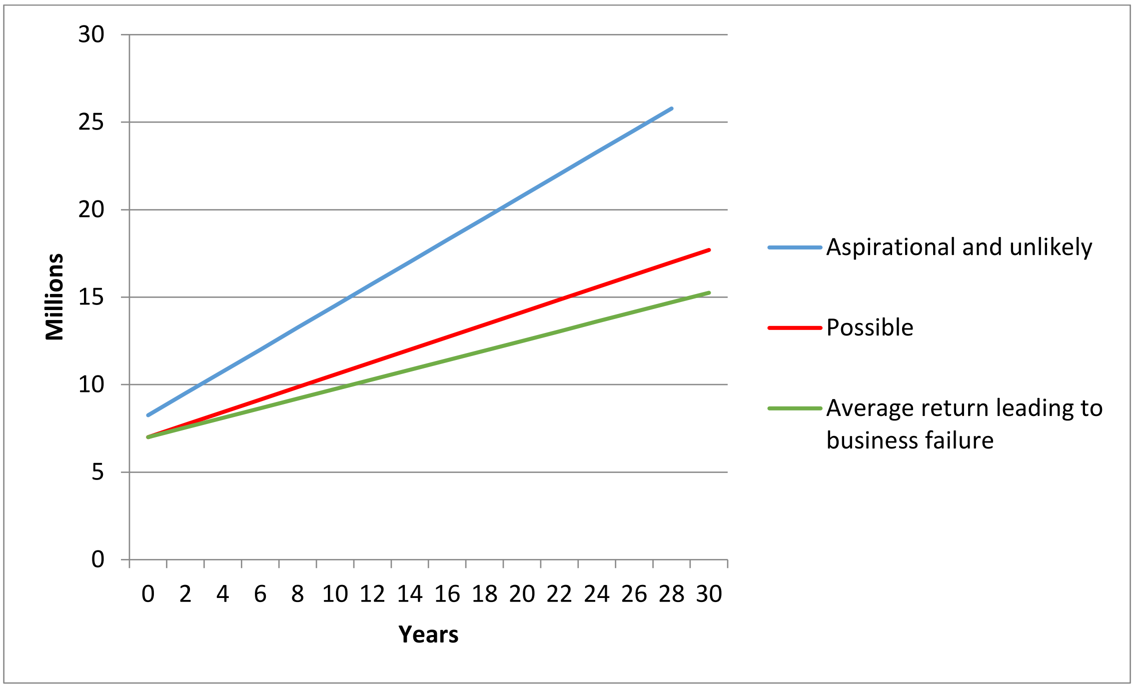


Table 3. Current and future assets

Case Study name Time frame

Description Values from the balance sheet	Current situation current $	Future situation future $	Future situation current $
Land assets			
Stock			
Plant			
Other			
Liabilities			
Net assets			

The possible, most likely wealth that could be accumulated at the end of the planning period is estimated, based on assumptions about future operating profit and return on capital and changes in asset values over the planning period. This is the key piece of information that informs much of the further thinking about what succession outcomes are plausibly within reach and realistic potential pathways to follow.

Contrasting Attributes of Families that Did and Did Not Achieve Succession

The contrasting attributes of the case study businesses which are or are not continuing and the people who own and manage them are shown in Table 4.

Table 4. Contrasting attributes of continuing and not continuing businesses

Business continuing	Business not continuing
An absolute determination to grow the business to enable succession	The belief that achieving the three main aims wasn't possible
Intelligent leadership	Autocratic, patriarchal behaviour
A history of well thought out succession	Poor history of succession
Progressive farm management	Doing things the way we always did
A focus on the customer	What customer?
The intelligent use of capital	Using capital to support the lifestyle
Preparedness to go into debt and maintain low equity	Totally debt adverse and maintaining lazy capital in the business
Deliberate strategies to woo stakeholders	A strategy of keeping them off farm and disengaged
Managing with humility and quietly going about your business	Maintaining your position in the family and society as somebody very important
A determination not to **live** like peasants	A determination not to **look** like peasants
A common end game goal	No agreement about the end game
Respectfully challenging advisors.	Threatening advisors.

Achieving the three main aims depends upon the attributes above, as well as:

- The success of the generation in control in achieving those aims.
- The aims of individuals in the next generation.
- The provision of choices for following generations.
- The success of the next generation in achieving those aims.
- The family accepted that the plan will always be a work in progress because:

   i. People change their minds.
   ii. Die unexpectedly.
- Unexpected circumstances, including poor seasons and markets and government policy, can create an environment that results in setbacks in the execution of the plan.
- Business owners in each generation started planning at a young age and had:
   i. Ensured family cohesion within and between generations.
   ii. Concentrated and worked hard.
   iii. Employed or retained the best people available.
   iv. Grown the business steadily.
   v. Managed family expectations.

Implications of the Findings

For succession of a family-owned broad-acre farm business to work out successfully it needs to be a continual part of the overall strategic planning of the family and the business. It is a long-term process, and a dynamic one subject to changing circumstances – it is not an unplanned, add-on *ad hoc* factor to be dealt with 'when the time comes'. In many families the claim is made 'it's too early to start succession planning because the kids don't yet know what they want to do.' While uncertainty about the aspirations of offspring is often real, sometimes until the potential farmers are into their 20s, it is never too early, or too late, to start planning for succession. As the saying goes: 'the best time to plant a tree was thirty years ago; the second-best time is now'.

There are seven first-order queries to raise with family members about planning for succession:

1. Do you want the farm to stay in the family?
2. What is the capacity of the farm business to generate income?
3. What is the family net worth and what percentage of the family capital is involved in the farm?
4. What is the debt/equity position of the farm business?
5. Does the older generation have sufficient resources to allow financial independence which does not involve the farm business?
6. How many children do the older generation have?
7. There are two extremes in relation to the issues relating to the fair, equal and equitable eventual distribution of the family wealth. At one extreme, the net wealth is divided equally amongst the children. At the other end of the spectrum, the farmer(s) are allocated the funds required to ensure the business has reasonable prospects of continuing and the other child/children get what is left over. Each member of each family has to decide where they stand on this issue.

When working with clients in preparing a succession plan a sound process is set out below. Note that, while many professional succession planners commence the process with a family meeting, the experience at Meridian Agriculture is that such meetings early in the process are fraught with danger. The recommended process is as follows:

1. Meet with the family member who initiates the contact - usually the person/people who own the land.
2. Develop a planning proposal - usually showing a number of steps and go/no go points.
3. Document who is who in the family and develop a genogram (eg., parents, children, spouses, partners).
4. Describe the location, size, history, enterprise/s, financial situation and performance of the farm(s).
5. Conduct individual interviews with family members on a confidential basis.
6. Work with the family accountant to compile the facts and figures.
   i. Who or what entity owns which parcels of land?
   ii. Who or what entity owns water?

iii. What are the Capital Gains Tax implications of changes of ownership
iv. Inventory (of plant, livestock, fodder and grain)

7. Work with the family lawyer to develop an understanding of legal impediments.
8. Develop the best fit plan and present it to the parents, then the family and road test it: what if people:
   i. Die/divorce/become unwell unexpectedly?
   ii. Change their minds?
9. Draft the Deed of Family Agreement and work with the accountant and lawyer to ensure all documents are harmonised.
10. Finalise the Deed of Family Agreement.

The likelihood of a succession plan being accepted and adopted by the family is increased when a team of professionals is assembled that not only considers farm management, people and relationship issues, but also the legal and accounting aspects of the plan. Each of these professionals operating in isolation from the others carries a degree of risk. Many accountants and lawyers who purport to prepare succession plans ignore many of the 'people issues' and create business structures which are difficult to 'undo' and are sometimes principally tax-driven. Often the lawyer and accountant will take advice from their client (usually the older generation) who supports or suggests the proposed plan, but without the younger generation being consulted, let alone having the opportunity to understand or endorse or otherwise the plan.

Conclusion

In summary, achieving the three main aims of farming for succession - providing adequate funds for retirement; providing a viable farm for the next generation; and providing a fair share of family wealth to all family members, including those who are not involved in farming - is difficult, and takes a long time. Achieving all three aims is uncommon because it is so difficult. The reasons are many and complex, ranging across the economics and finance of farming, the scale and medium-term profitability of the business, planning and intent, and complex interpersonal family relationships.

To achieve these three aims, farm families need to start building the business early in life, work hard, consistently perform well, keep the family engaged, have a plan and maintain open and honest communication between all family members. It is never too early to start planning for succession. Planning for succession, farming well and grasping opportunities that emerge are necessary to achieve the size of farm operation in which succession is a choice. Scale is important but scale alone will not enable the achievement of the three main aims. Rather, to do so, the older generation has to be prepared to let go, the younger generation has to be prepared to take over and the whole family has to be satisfied with the result. Consistency of purpose is the key.

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