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How Do You Plan for the Cost of Succession?

By John Hewlett, UW Ranch/Farm Management Specialist

Most people look forward to retirement with anticipation, often imagining it as the end of their working life. In many cases, the retiree does not plan to worry much about financial planning and investing after retirement. A recent *Forbes* article describes the reality as far different. "Forty percent of baby boomers expect to work until they die, according to data from AARP." In order to retire financially secure, you must have a plan. But what should it include and how do you put it together? Are there other details we should be worrying about; which ones?


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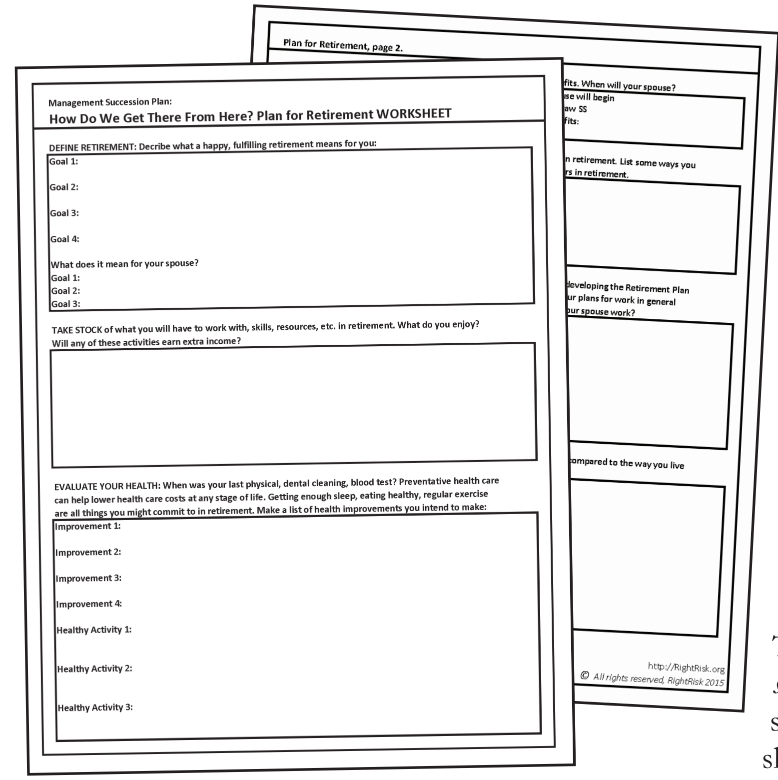
Bertha and Joe had planned to retire in their early to mid-60s since they bought their last farm. They were both now in their later 60s and didn't really have a solid plan for transferring the farm or the management duties to either of their two children. Sally and Billy Joe had both been back on the farm since completing their college degrees. The farm was doing well and the three families seemed to have good communication. However, both Sally and Billy Joe had concerns about their parents retirement. In particular, they were worried about the financial management of the farm. Bertha had always kept the books and neither she, nor Joe were very interested in sharing any of the details. The questions hanging over the farm these days was, "When will they retire?" and "Where will we stand financially when they do?"

Retirement Plan

It is vital to lay-out the specific steps needed to move the present managers from day-to-day management of the farm or ranch to full time retirement and transition the new manager (or managers) to full authority, so that they can begin to plan and prepare for the next successors who will carry the operation on into another generation.

Retiring managers often must rely on the business for support during the later stages of life. Oftentimes, so much money has been invested in the farm or ranch, that no savings, investments, or retirement funds have been established for those who are at the retirement stages of their lives. Financial preparations should be made to accommodate retiring founders as well as the successor(s) transitioning into management. If necessary, talk to financial, investment, and retirement planning experts.



When considering retirement, it is important to estimate your financial requirements. Retirement can be expensive. Most experts estimate that retirees will require 70-90 percent of their pre-retirement income after they stop working. In short, paying for the retirement you truly desire is ultimately your responsibility. This is another reason why it is beneficial to plan for retirement while you are still young.

Specific steps to consider in preparing for retirement include drafting: 1. A financial plan showing how retirement will be financed; 2. An agreement between the retiring manager(s) and the successor(s) about the extent of involvement the older generation will have in the business; 3. An agreement about where various farm family members will live; and 4. Some ideas about what activities will absorb the retiring generation's creative energies.

The *Management Succession Workbook* from the *Management Succession: How Do We Get There From Here?* online course includes a section on Retirement Planning. This section provides a worksheet allowing users to begin sketching the details of a plan: when to retire, ideas on how long the process might take, what your biggest concerns are, etc. Budget planning sheets are also included to help consider what personal expenses might look like in retirement, as compared to their pre-retirement totals. A resource section provides links to other helpful online financial planning materials.

Financial Plan

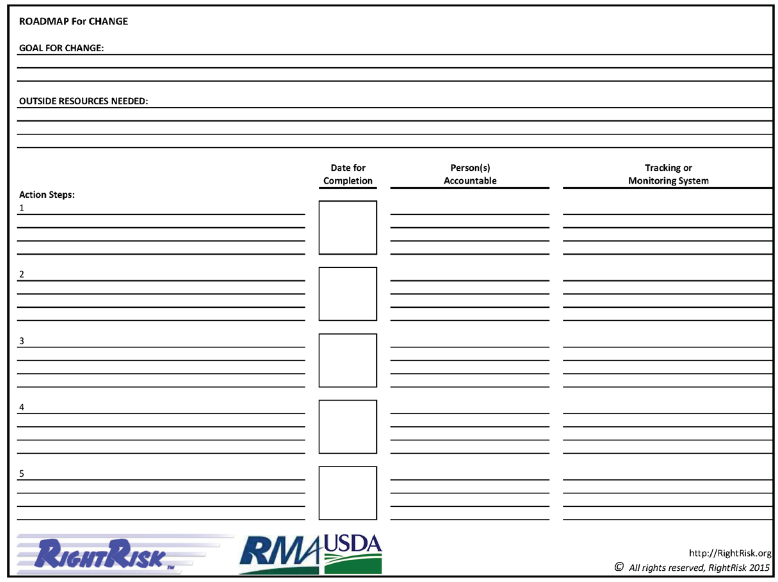
Very few people ever have enough money to cover all of their wants in retirement. It seems that the more we have, the more we want and think we need. But the power of choice can control incomes of all sizes. Setting financial goals gives a person that power. Determining the sources and amount of cash flows is the first step to matching our cash inflows to our cash outflows. Families experiencing difficulties and expressing concerns about money often lack information and plans for managing the money they have available to spend.

The Financial Plan Worksheet from the *Management Succession* course offers a place to begin outlining a brief summary of the financial plan for the business. Although a much more detailed version could be compiled, this worksheet is intended to provide the financial highlights for the transition. The value here is that it will help to answer the following questions: Has a management succession assessment been completed? Have the business strengths/weaknesses and opportunities/barriers been assessed? Has a Roadmap for Change been drawn up to outline the steps to reach the goals of the farm/ranch? Links to additional financial planning resources are also provided to help move beyond the initial draft.

Documenting Your Financial Assets

You will want to designate someone to handle your financial affairs, including paying monthly bills, when you are no longer able to do so for yourself. You will need to allow that person access to your bank and other financial accounts. This is commonly accomplished via powers of attorney and ownership of joint accounts.

Assets can be defined as anything owned by you or your business that can be sold, traded, or otherwise has value. At this point in the calculations, it is irrelevant whether or not there is any debt against the assets.


ROADMAP For CHANGE

GOAL FOR CHANGE:

OUTSIDE RESOURCES NEEDED:

Action Steps:	Date for Completion	Person(s) Accountable	Tracking or Monitoring System
1			
2			
3			
4			
5			

http://RightRisk.org

Assets are classified as either current or long term. In agriculture you will sometimes hear discussion of a third category, called intermediate assets. Asset categories include:

1. Current assets are those which generally have a useful life of less than one year. Such assets are liquid (i.e., they can be sold or easily used within a very short period of time). Some examples are cash, checking account balances, and feed inventories.
2. Long-term assets are those with a useful life of greater than one year. They are not typically liquid and the sale of such items would impact the revenue-generation process. Examples include real estate, buildings and equipment.
3. Intermediate assets are somewhat liquid but their sale would impact production and future revenue flows. For example, breeding livestock might be considered an intermediate asset, rather than a long-term asset. Cows can be hauled to town and sold at auction, but their sale would reduce production and future cash flows.

Assets can be valued at: 1. Fair market value – what the asset can be sold for on the open market and 2. Net of depreciation – the purchase price less depreciation taken in previous years.

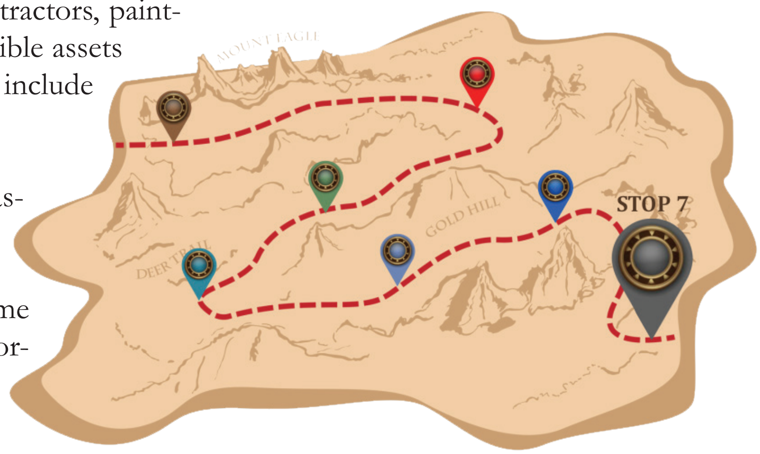
Liabilities are any debts, obligations, or other commitments pledged to someone else or another business. There are two categories of liabilities: 1. Current - obligations owed within the nearest 12 months and 2. Long-term – obligations owed beyond the nearest 12 months

Your net worth is the total value of what you own. It is calculated by subtracting your liabilities or debts from the total value of your assets. Net worth is also known as equity. A statement of net worth is also known as a balance sheet or statement of owner equity.

Real property are assets including land, buildings, and other permanent improvements which are fixed to the land.

Personal property are those assets not considered real property. Cars, bank accounts, wages, securities, a small business, furniture, insurance policies, jewelry, patents, pets and season baseball tickets are all examples of personal property. Such assets may be thought of as movable. There are two categories of personal property: 1. Tangible assets are personal property

that can be held or touched. A few examples include horses, tractors, paintings, and a doll collection. They may be depreciable. 2. Intangible assets are personal property with no physical existence. Examples include stocks, bonds, etc.



Financial managers will require a comprehensive list of your assets and liabilities, allowing them to calculate your net worth and track how it changes over time. Real property and personal property are two different types of assets. There are some unique issues to consider when transferring real property. In order for someone to take over management of your financial accounts when you die, he or she will need a list of all your assets and liabilities.

Contingency Plans

Every succession plan should include contingency plans. What will happen if something goes wrong? Under this heading things like disability insurance, life insurance, employee training, back-up support, how-to manuals, and communication with family, employees, and key stakeholders should be considered.

Sometimes, when on a trip, we run into road construction or a washed-out bridge and are forced to replan our route. We may not have all the answers when we first encounter a failure or major roadblock, but we should have a process in mind to deal with such situations and to plan a new route. Again, communication is critical in dealing with contingencies.

Sometimes we just can't get there from here. If the roads and bridges are totally destroyed, we may have to settle for a new destination. Consequently, every strategic plan needs a system for changing the course of action when obstacles appear in the path forward. Never assume things will go just as you planned – they seldom do.

It is critical to ensure that all members of the business are committed to the succession plan and understand what headway is being made toward accomplishment. To make sure this takes place, regular meetings should be scheduled and family members updated on progress. If needed, replanning or adjustments to the overall direction, roles, responsibilities, and timeline should be made to allow the succession process to proceed to the desired outcome.

The main thing here is to ensure that everyone involved is still committed to the same journey. If major changes have occurred and individuals feel it is needed, it may be necessary to revisit all the stages planned for the journey to ensure that the business and the people involved arrive at the destination.

An online module, including a recorded presentation covering growing relationships with the next generation, and other information on developing your management succession plan is available at our website. For more on upcoming modules, past newsletters, and for information about Ag Legacy see **AgLegacy.org**. Requests for additional information may be emailed to Information@AgLegacy.org.

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