

**EFFECTIVE OWNERSHIP STRATEGIES: THE KEY TO FARM FAMILY BUSINESS SUCCESS OVER TIME.**

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Ownership has the potential to make or break a family farm business and farm family, yet has long been the neglected area of family farming in Australia.

A lack of understanding of the effects of ownership, by both farm service providers and the farm family, can result in the following:

Turn a viable family farm business into a non-viable family farm business OVERNIGHT, due to a family crisis and particularly, at the time of farm succession.

2. Due to the traditional process of the son/daughter, who receives the farm and paying out siblings their share of inheritance, leaves a family farm business in a liquidity trap, which will significantly impact the future rate of, and uptake/use of recommended applicable agricultural, environmental and business innovations/technology.

*All family farm businesses need to grow to keep up with inflation, for providing for increasing cash needs as the farm family grows, both in number and age, and for providing farm family members business opportunities. Traditionally, partnerships and single ownership structures have been used. These structures, whilst cheap to set up, may be costly and difficult to exit and are inflexible for growing the family farm business and intergenerational transfer.*

• *The Rural Industries Research and Development Corporation (RIRDC) provided the funding base for developing, "Techniques for the Growth of the Family Farm Business". Ownership comprised a major focus of the research undertaken.*

The family farm comprises three (3) major components, farm business, ownership and farm family, which are serviced by different farm service providers. Ownership is the LINK between the family and their farm business.

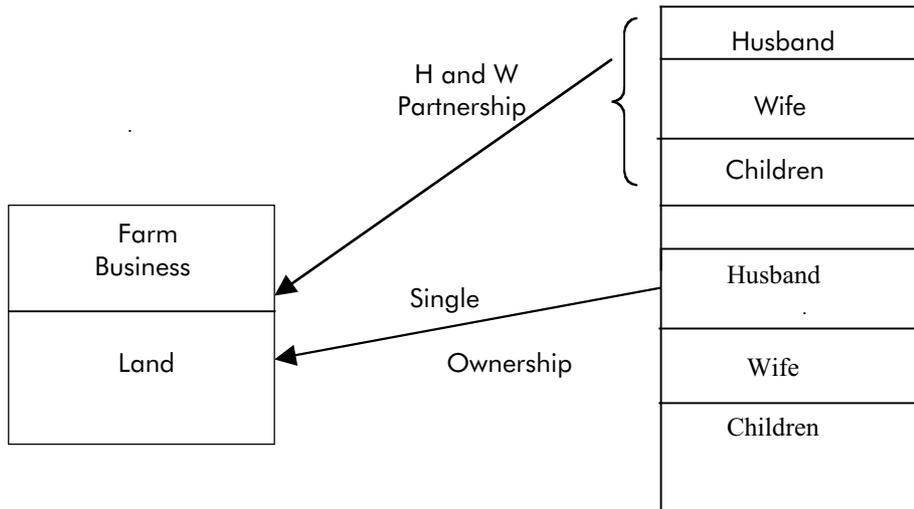
Each of the sectors needs to be reviewed separately and then combined. The following model formed the basis of the research project.







**Figure 3: Type A. Separate ownership structures for farm business and the land.**



**Land.** Partnerships, trusts and companies, as well as single ownership may be used. Need to look at the future possible ownership positions, before deciding on an ownership structure. Sibling arrangements (as tenants in common) can substitute for a single family position in this model example.

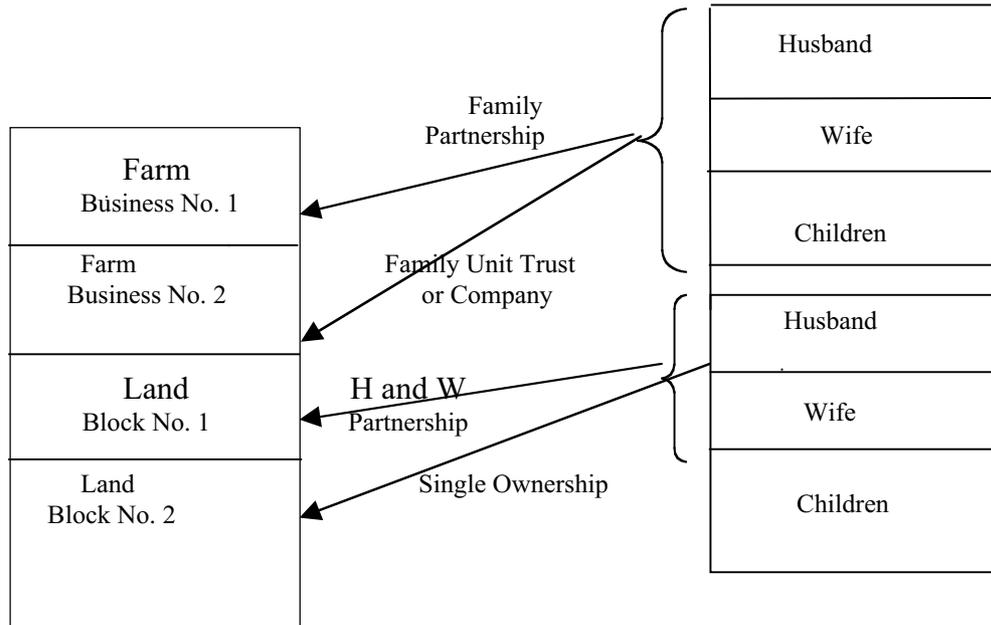
**Farm business.** Single proprietorship, trusts and companies, as well as partnerships. If land is owned as single ownership, then ownership of farm business must be other than single proprietorship or two different individuals involved. For children to be included in the H and W partnership, then a new partnership is formed, involving CGT in some way, if property other than trading stock and depreciable items are involved. Sibling arrangements can substitute for the single family arrangement in this model example.

Note: Involving a son or daughter in a family partnership will involve the following decisions:

- Legal arrangement: tenants in common and or joint tenants.
- Financial arrangement: Gifting or purchase a share. Gifting only spreads the profit generated between more individuals and does not increase the capital or grow the farm business. Paying a minimal wage to the younger generation partner is really a way of this partner buying their partnership share over time.
- A written partnership agreement.

**Figure 4: Type B. Multiple family farm businesses.**

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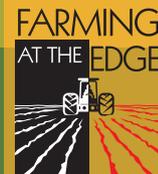


More complex arrangement developed from the type A model above, which allows for ownership flexibility for farm business growth and retains asset security by parents. More complex models may be developed provided the **PURPOSE** to be served is clearly set out

***What is the purpose to be served by the selection or review of present ownership strategies? Ownership strategy is a MEANS TO AN END and not an END IN ITSELF.***

The purpose to be served by the ownership strategy is vital for both the farm business and the farm family. "I think with any of these structures, it has to be so built, so that you can get out before problems start – I think it comes back to the point I was making earlier, that if people have an aim or goal and they use that and when it is finished, its finished." Workshop participant comment.

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What needs to be considered, i.e., involvement of son/daughter in the **ownership** of the family business, setting up of a separate company for another business, e.g. grain trading, changing ownership legal structure, superannuation trust, partnership with brother/sister/parents, syndicate, keep land separate to business, etc.

- i \_\_\_\_\_
- ii \_\_\_\_\_
- iii \_\_\_\_\_
- iv \_\_\_\_\_
- v \_\_\_\_\_

**Then RATE important factors to be involved on the NEXT page.**

**CHECK LIST OF WHAT YOUR OWNERSHIP STRUCTURE NEEDS TO PROVIDE YOU**, i.e., issues that may need to be considered when reviewing the usefulness or adequacy of your present ownership structure; or if you are looking to change or set up an ownership structure for your business or anticipated business.

Rate the importance of the following to be achieved by the legal ownership structure.

		<b>Very important</b>					<b>Not important</b>
		1	2	3	4	5	
1.	Security for parents						
2.	Allow growth in business through equity capital						
3.	Allow for off farm income provided to business to be recognised						
4.	Flexible legal structure						
5.	Confidentiality of business financial position						
6.	Minimise capital gains effects when membership of business changes						



**How useful is an 'Ownership Structure comparison, of advantages and disadvantages'? Mail survey respondents response to a list setting out the advantages and disadvantages of single proprietorship/ownership, partnerships, trusts and companies.**

Not important	1	2	3	4	5	6	7	Extremely useful.
<b>Actual</b>			<b>3</b>	<b>6</b>		<b>21</b>	<b>=</b>	<b>30 Mean 6.6</b>

**How useful is information on the different types of trusts (discretionary, fixed and unit trusts), formation of trusts and the important component of trusts? Mail survey respondents response to information provided, including a diagram of a unit trust structure using a trustee company as trustee.**

Not important	1	2	3	4	5	6	7	Extremely useful.
<b>Actual</b>						<b>2</b>	<b>7</b>	<b>21 = 30 Mean 6.63333</b>

**What problems may be caused by a lack of understanding of the various legal and strategic aspects involved in using ownership structures? Case examples from the literature and research project.**

**Case 1.** Harvey v's Harvey 1970. (Also covered by the ABC's Australian Story, "Buying back the family Farm"). Two brothers formed a partnership and farmed land, owned by one of the brothers, which did not become partnership property. The other brother with his sons built up the farm over a number of years. When the partnership terminated, this brother's family sought their share of the improved value of the farm only to find he and his sons had worked to build up the farm assets for the other brother. The partnership basis was 50% of profit.

Vital to have a partnership agreement, which is fully understood and negotiated.

**Case 2.** Family farm partnership of parents and married son with 1/3 shares-assets and profit. Father died and left an out dated Will. Parents share of drawings significantly exceeded partnership agreement, with son's ownership share exceeding the partnerships net assets. Family only interested in the fathers Will distributions, which would involve the father leaving assets under the Will that he did not own at date of death, due to parents partnership debt. Partnership used land purchased by partnership and land in fathers name.

**Case 3.** Parents owned 2 farms and 2 sons in their 20's. Parents were looking at a trust arrangement and accountant suggested that he, the accountant, be made the trustee.

**Case 4.** Trustee ignored fiduciary duty and beneficiary rights. Several properties and livestock left in testamentary trust for 2 children. When children reached the age they were to receive the property, only a small amount of livestock remained.

**Case 5.** Two sons farming with parents. Whilst sons were single, parents only provided money that the sons requested. When one son married he was paid a wage, then daughter in law requested back payment for wages not paid to her husband, but payment to take the form of transfer of land. Parents did not transfer land as requested, as did not know what to do, and grandparents not allowed to see grandchildren.

Seventeen (17) case situations, all different, were examined within the research project. Fifteen (15) of these cases involved lack of knowledge of ownership and what questions to ask or options that were available to them. In several case situations the advice provided the farm families was inadequate.

Is there a relationship between innovation, ownership, inheritance and the rural adjustment problem?

Numerous innovative ideas and techniques will be incorporated into a family farm business during the parent's lifetime. Then when the family farm is to be transferred to the next generation, inheritance becomes a major issue. Splitting the family farms assets between all family members is a parents assets **inheritance plan** and not a farm business succession plan. Inheritance may well be a major cause of the rural adjustment problem, which continues to plague successive federal governments. There needs to be an alternative to the traditional options offered farm families by the service providers.

Innovative ideas should cover intergenerational aspects, as well as the present major focus on intragenerational aspects of the family farm business. What is the preference of parents?

Prefer to give children an inheritance	1	2	3	4	5	6	7	Build on what parents have developed.
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i). Dimboola Seminar respondents

<b>Actual</b>		<b>1</b>	<b>-</b>	<b>2</b>	<b>9</b>	<b>13</b>	<b>21</b>	<b>19</b>	<b>=</b>	<b>65</b>	<b>Mean</b>	<b>5.64616.</b>
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ii). Mail survey respondents.

<b>Actual</b>		<b>1</b>	<b>4</b>	<b>3</b>	<b>6</b>	<b>8</b>	<b>=</b>	<b>22</b>	<b>Mean</b>	<b>5.72737</b>
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Parents are seeking alternative strategies to one strategy presently suggested to parents, ie., hand the \$1 to 1.5 million AUS farm over to the sons/daughters and take a pension. Many farm parents are not interested in this option, but say they do not know what else to do! “\_ many important issues that family farms/members need to discuss, but often don't due to lack of knowledge and an attitude that things will workout”. Parents are also seeking an alternative to the inheriting son/daughter buying out siblings.

“\_ the idea of each generation having to buy the farm – having to ‘buy out’ a brother – makes sense of the question why so many farm families that have been farming for three generations have been struggling – so the son inheriting the farm and buying out his brother(s) is really in no better position than the previous generation. The idea of helping the children into

horizontal business opportunities makes more sense than gifting all the land to one or two and then expecting them to fully appreciate their windfall.—There needs to be some new thinking in terms of business structures to allow the million-dollar asset to provide a better standard of living for farm families”.

“In my local community I have seen the vast majority of family farms end up having their business base severely dented by succession issues not to mention family relationships”.

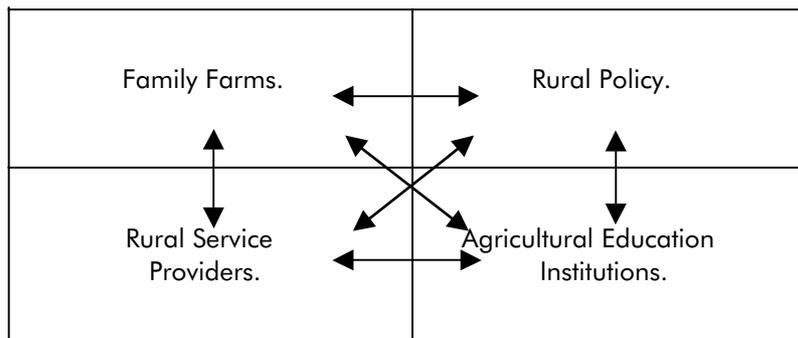
“Why this obsession with treating all the kids equally? If one or two put their whole life (so far) and the others have been educated (the farm paid for this)\_and have their own lives and no interest in the farm, why should it be split up to pay them out? Too many farmers have got into serious, inextricable debt over this kind of practice!”

***Intergenerational option of using a unit trust.***

“One of the issues that greatly interested me was the separation of the land from the business. At first I was reluctant to see how this could work as it was against all that I have seen and brought up to understand. But through this growth it has made me see how a ‘landless farmer’ can build up a business and be successful, expanding to own their own land. In separating the land from the business I particularly liked the idea of the trust situation. Both (my husband) and I were opened to the idea of a unit trust for the business when (eldest son) will be old enough to be included. This would ensure the ongoing safety and viability of the business and allow (another son), in later years to become involved without the disruptions of a new partnership whenever the change was required”.

“Not sure on this one. I like the idea of a trust (perpetuality especially) but what if the government changes the tax rules. How do you value the units? Who has control?”

**• Is the following relationship possible? Who is the ultimate client?**



Adaptation of the equilibrium model used by McClelland and Winter (1969), p. 359.

“I think it is a good idea and will ensure older generation retirement will also strengthen the Australian farming industry”.