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This is one of a series of articles written by Dr. David Kohl for the Minnesota State Farm Business Management Education Program.
Vol. #110

Business Transition: The Marathon

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From the quarter-century mark to the year 2040, business transition in American agriculture will be front and center in strategic plans. However, business transition will also be the central focus in America as the baby boomers move through various phases of retirement. As stated in a previous article, over $68 trillion of assets and equity in the U.S. economy will transition in a 15-year period. Currently, females own approximately one third of those assets; however, by the end of 2040, women will own nearly two-thirds of the assets and equity. This is a result of women outliving men by an average of seven years, more women owning and managing businesses, and more women investing in retirement accounts. One only has to conduct a windshield appraisal of the agricultural landscape to provide evidence to support this trend. The predominance of more “granny” landlords and businesses owned by elderly females that are managed by farm management firms and other consultants are becoming more prevalent.

Transition traps

One has to separate estate planning, the transfer of assets and equity, from business transition, the evolution of management to the next generation of owners and managers. In the latter case, more family businesses are transitioning to non-family members. Other businesses are being transitioned to family members that involve cousins or more distant relatives that require another degree of complexity in the transition equation. About 21 percent of business owners have no next generation to whom they can transfer their assets and equity. What are some of the estate and transition traps that are being observed?

Having a basic will is often overlooked, even with larger businesses. For example, a recent visit to a large agricultural operation came with a big surprise. As we sat around the kitchen table, one of the first questions was, “Do you have a will?” The owner, who had just turned 65 years old and has $17 million in equity, responded with a guilty look. His nonverbal communication was a clear “No!” Turning to his wife, the same response was enumerated. In this case, with four children and stepchildren, their death could result in opening a huge can of worms and much more complexity in order to continue operating a very successful business.

However, this couple does get credit in the transition and estate planning marathon. He had a life insurance policy initially set up four years ago with proceeds from the policy set up to pay off the farm's debt. However, there was no clear direction as to where any remaining funds would be directed. In addition, his wife had no life insurance and was very instrumental in the management of a 10-person workforce and conducting outreach activities with the public, which is critical to the business' profitability.

The next transition trap is control. In this case, and like many in agriculture, this couple's life's work was building a successful business with some equity that was earned and some that was a result of appreciation. His biggest fear was that if he developed an estate plan, a will, and particularly a transition plan, he would be giving up control, which was in opposition to his very dominant personality of being oriented toward the control side. The "control freak" is a common challenge in the agriculture transition process. In this case, the control freak is the owner or manager, but in many cases, it can be a grandfather or grandmother who sacrificed and experienced the roller coaster of economic cycles that have yet been experienced by the younger generation. They often have concerns about the younger generation's ability to withstand economic cycles.

For those of you facing this issue, the following are some words of wisdom. In the transition marathon, you must give up control to maintain control. Failure to do so can result in a very emotional phase in the process where forced decisions must be made by individuals who may not have the expertise or experience to continue the business or divide the assets and the equity.

Next, be careful! The lack of a transition plan can result in a financial liquidity trap if a negative trigger event were to occur. For example, without proper planning, sudden death, disability, sickness, or other life-changing events can result in both a financial and business disruption. Sixty percent of lifetime healthcare costs occur in the last six months of life. Children who previously showed little interest in the business may suddenly want their share of the appreciated assets and they want it now. The business often must cover medical bills, costs, and the loss of key owners and managers which can change the profitability equation very quickly. If no plan is in existence, individuals or family members in the business often have to buy out others at inflated asset values. With the volatility and uncertainty facing the industry, this situation can create a tremendous dilemma. If one attempts to create equality for all family members, including those inside and outside the business, it often results in the fragmentation of the business into smaller pieces that are uneconomical in size and scale to be profitable. When solving this issue, long-term healthcare insurance policies must be analyzed, addressed, and examined. In most cases, this should be completed when individuals are between 45 and 60 years old and before health challenges occur to avoid costly insurance or being uninsurable.

Life insurance proceeds payable to nonfarm siblings is another method of circumventing the liquidity issue. These proceeds are in cash with no risk, maximum flexibility, and can fund the non-farm siblings' portion of the estate. Life insurance on senior partners can also provide a financial liquidity bridge for a smooth, seamless transition of the business to the next generation. Engage professional advice to ensure goals can be met using the aforementioned legal and insurance products.

Final tips for managing the marathon

One of the first steps is to have all major stakeholders outline written goals. This can include business, family, and personal goals as well as mental, physical, and spiritual goals. Short-term goals are focused on less than one year and long-term goals are between three and five years. The key is everyone must complete this exercise individually and then have a facilitator or farm management instructor summarize the results. Build on the commonalities and negotiate out the differences in the plan.

Communication is often an issue in estate and transition planning. The DiSC personality assessment can be a tremendous tool to assist in understanding the different communication styles in a family or with non-family members.

Hire a facilitator! Remember, this process is not a cost, but an investment both in money and time. The facilitator will establish agendas, summarize minutes, and function as a coach or teacher in helping you through the marathon. Often, the transition process will be put on the back burner if there is a lack of guidance from the outside.

A professional team includes an agriculture-oriented lawyer, accountant, and financial planner. I suggest that everyone meet together off the business premises. Some of the more successful transitions I have observed and worked with are when the team is placed on a retainer rather than paid an hourly compensation. For example, the project is outlined and a cost is set. However, any changes are analogous to building a barn, shop, or a house and will result in a change order which will influence the cost of the professional team.

The signing of the documents is analogous to a marathon runner hitting the proverbial wall! It will be the most difficult emotional aspect of the process you will conduct. Remember, to maintain control, you must give up control. Otherwise, the future of the family and the business celebrations will be on the line.

The marathon of business and estate transition will take time and requires a step-by-step process to have a successful business, family, and personal transition outcome. The key is to execute and monitor the process all the way through to the finish line.

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