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Tough Talk about Transition

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This past year, I conducted nearly 20 young and beginning agriculture producer conferences in person and virtually. Some were multi-day events, which were very conducive to engagement and discussion. At these events, the young farmers and ranchers were asked, "What keeps you awake at night?" The usual suspects such as weather, prices, inflated costs, and interest rates increasing were often mentioned. Some indicated it was explaining special circumstances of operating a farm with a nonfarm spouse or partner. However, the number one worry on the list was transition and estate planning. Digging deeper, it was the lack of communication or failure in the whole process. Some indicated that the senior generation was holding them hostage in their attempts to plan for their roles and growth in the business. With this as a backdrop, let's talk candidly about the tough subject of transition planning. Along the way we will intersperse some of the tips and tidbits of wisdom gathered over my decades of working with businesses in this area. I will intersperse some survey results from a recent session conducted for Tennessee Cooperative Extension called *Transitional Turkey Talk*, which was done during the two days before Thanksgiving.

When the Tennessee producers were asked general transition planning questions, 12 percent indicated they were start-up operations, 16 percent were the first generation, 4 percent were the second generation, 36 percent were third generation, and 32 percent were at least the fourth generation. One in three small businesses, including farms and ranches, are second generation nationally. According to a *USA Today* article, the odds of reaching the six generation are 500 to 1 and European farmers have about a 40 percent exit rate after a five-year period of being in a family business. I am proud to say that one of my former students, a Virginia Tech graduate, operates one of the oldest businesses in the United States. The company is over 400 years old and is now in the 11th generation going on to the 12th generation. There is an old saying that the first generation makes it, the second generation holds it, and the third generation loses it. This is because production practices are often passed down, but many times business and financial management skills are not taught to the next generation, they are passed on too late, or poor management practices are transitioned.

Generations in business

The participants were asked how many generations were actually involved in the transition decision-making. Over half indicated just one generation was involved. However, nearly half indicated that two to four generations were involved as people are living longer with more active lifestyles. Attempting to integrate multiple generations with different generational perspectives often complicates the transition management process or situation.

Obstacles in transition planning

Obstacles and challenges are always prevalent in the transition planning process. The Tennessee producers were asked to rank the challenges. The top response was motivating people, followed by having time to complete the process. These responses were listed by 60 and 50 percent of the participants, respectively. Forty percent of the respondents noted that transition planning is not seen as a priority and 30 percent listed that overall communication was a challenge. Interestingly enough, the cost of the transition planning process was only enumerated by 12 percent of the producers. If you were to complete this survey, how would your responses compare to the good ol' Rocky Top group?

Does transition planning payoff?

A former graduate student conducted a study to determine if transition planning paid off. The return on assets (ROA) for farm businesses with a documented transition plan was two percent higher and net profits were $60,000 more. Drilling down, the ROA was nearly three percent higher and net income was almost double for businesses that had a formalized estate plan.

The transition planning process

There are three critical steps in the transition planning process:

1. How do we get started?
2. How do we keep it going?
3. How do we get over the finish line with signed documents?

The transition planning process often gets started after a trigger event such as a death or accident in the family or community. Sometimes it is a seminar, podcast, or even an article like this one. The first step is to conduct a "drop dead" exercise, which is often used in the military. Place the names of the stakeholders in a hat and randomly select a name. This person is "dead," now what do you do? Do not be surprised if the "dead" person attempts to speak.

Oftentimes this person must be dismissed from the discussion. Be prepared for surprises such as the loss of the youngest generation or the newest member of the team.

To keep the transition planning process going, I highly suggest investing in a facilitator. This could be a farm management instructor or a professional consultant. A facilitator acts as a coach to outline agendas and minutes from the meeting and encourage discussion. If you do not consider firing this individual at least three times during the process, they are not asking the tough questions!

Finally, getting over the finish line will often require one-half to one percent of your assets or equity and 100 to 200 hours of time in total. Conduct your meetings with all of the critical professionals in attendance. Place these individuals on a retainer, rather than an hourly basis. Be prepared to invest time and money. Have all of your important documents such as deeds, wills, financial statements, and loan agreements available to reduce the overall cost.

Tough talk and wisdoms

Have the senior generation develop a history of the business. This is a great way to get the process started and to get buy-in. Use videos and the latest technology to capture key points and to present to future generations. Have them discuss challenges, successes, and their institutional memories which will be very critical for navigating the business and economic cycles in the future.

A personality profile of each stakeholder, utilized by some of the more prominent transition programs, is very critical. This will assist in communication. Knowing that some individuals will be direct, others will be analytical, some will be steady, and the rest will be outgoing can accelerate the process. Do not forget that transition teams such as accountants, lawyers, lenders, and facilitators need to go through the same process to improve communications.

Tough Questions

- Does the business generate sufficient income on an accrual income statement to support the transition process? Do not use a Schedule F tax form designed to minimize taxes.

- How are the senior generations' income requirements going to be met? The answer may be a combination of the sale or lease of the business, Social Security benefits, and retirement accounts.

- Where are the senior and junior generations going to live?

- Does the senior generation have long-term healthcare insurance?
- What are the junior generation's roles, skill sets, and the value of compensation packages, including fringe benefits?
- What about the family members outside the business? Remember, you cannot treat all family members equally. Fair and equitable is the name of the game.
- What is the business culture, the quality of business assets, and the business' competitive position in the industry?

This is just a sample of the tough talk and crucial conversations required in the transition planning process. Please see the updated Sweet 16: Golden Rules of Transition Management assessment to determine where you are in the process.