Lead Your Family In Ownership Transition

Here are four conversations you need to have with heirs.

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Multigenerational family farms and ranches face important decisions about their futures. Some decisions focus on how the business will grow or adapt to changing markets or new opportunities. Some decisions have to do with who will eventually lead the business. Yet another set of decisions determines how the business—the land, livestock, inventory and equipment—will be owned in the future. Here are the ownership conversations you should have with your spouse and as a family.

1 Who will own the business? There are two levels upon which to consider this question. The first is on-farm owners versus off-farm owners. Should all siblings inherit business assets equally regardless of their involvement in the enterprise? This may solve the parents' goal of treating the next generation equally, while simultaneously creating problems and conflict by mandating a business relationship between your adult children who don't work together.

The second level of ownership relates to the differing amounts of time spent by the younger generation working in the family business. Should everyone own equal proportions of the business, even if some have worked there longer than others? Equal ownership may create resentment by those who have invested more time in the business, but a differentiated ownership structure can feel punitive to those who were born later and, by no fault of their own, can't catch up to their older siblings' years of service.

2 How will the ownership transfer occur? Outside of agriculture, small businesses are often sold to finance the senior generation's retirement. But, in agriculture, the capital intensity and generational buildup of wealth, the opportunity for land rent to provide retirement income and the potential estate tax lead most families to gift assets to the next generation. When families don't specifically talk about this "gift or sale" question, people end up guessing or assuming an answer. The assumption of a gift can give an impression of entitlement. And, with an intended sale of some assets (for example, equipment), a window of time for tax planning and financial preparation is beneficial. A conversation well ahead of a transition is helpful to all.

3 When will the ownership transfer occur? If the ownership transition will happen upon the death of the senior generation, the "kids" who inherit the business may be retirement age before they become owners. Many family members resent the fact that when they inherited the business, it was time for them to consider passing it on to their kids. They never felt like owners. But, if the ownership transition happens before death, the senior generation may find it hard to give up control. Finding the right time to start the transition is hard.

4 How do partners get out of business together? When business ownership transitions from a two-person parent structure to a next-generation sibling partnership (with in-laws nearby), the odds are high that someone will eventually want to exit the partnership. A thoughtful approach to potential exits is one of the best gifts the senior generation can offer. Should a selling partner's equity be discounted? What terms protect the business while not creating animosity between siblings? How will assets or company shares be valued? There are no cut-and-dried, easy answers to these questions, but there are models and examples that can help you tailor a strategy that fits your goals as a family business.

These discussions are difficult but necessary, and a "right" answer is elusive. Your job for many years has been to run the farm or ranch, or to manage the family assets. Now, your job also includes leading your family through an ownership transition. Tackling the four questions mentioned here with help from your professional advisers, if needed, can prepare your family business for a successful transition.

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