

## **Farm Succession Planning**

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### **It's All in the Plan**

The transfer of farming operations is often the most difficult issue for producers. It is both emotional and stressful, but also inevitable. Some producers have a natural succession plan with a child or children ready, willing and able to carry on the tradition. Others, for a variety of reasons, must look outside the family.

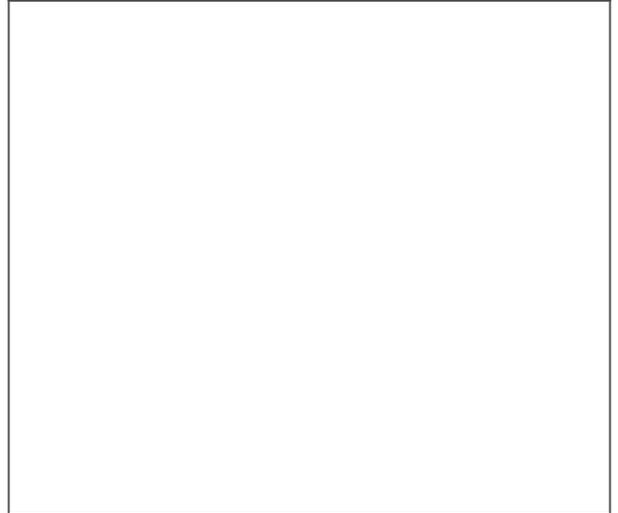
It is always best to have a transition plan established well in advance of the actual time of the transfer, which will address both expectations for all members of the family and the inevitable tax planning issues. It can also provide a focus for an orderly transition of the business as opposed to the perpetual “next year” syndrome.

As farming operations increase in size, so do the complexities in dealing with succession and tax planning. The age old practice of handing off the farm to the next generation is often no longer possible, let alone an option.

And while the size of the operations increases, the pool of available producers to acquire farming operations decreases. This is further exacerbated by the provincial farmland ownership legislation which restricts foreign ownership of farmland, thereby limiting the demand on the purchasing side.

As agriculture and its related value-added businesses become hot commodities in the world of finance, various land related pooled funds have been created with the mandate to acquire farmland. Whether or not you agree with the mandate or business model of these funds, they do provide producers another option who are looking to sell. And if price is an issue (and it usually is), options are good.

Succession plans, which are typically made up of both transactional agreements and estate documents (such as wills, trusts and powers of attorney), look at both the potential purchaser of the farming operations and the related tax issues. They can range from straightforward



and simple to very complex with many levels of legal structures in place. But if you do not have a plan and you do not transfer your farming operations during your lifetime, the law does provide your estate with limited tax planning options.

By law, if you have not sold your property during your lifetime, you are deemed to have sold it immediately prior to your death. This means that any increase in the value of your farming operations over and above the money that you paid for, and invested in, the business (known as your "cost base") will be a capital gain on which tax will have to be paid in the year of your death. From a taxpayer point of view, capital gains are good as only one-half of the gain is taxed. So if the fair market value of the operations was \$1,000,000 and you had invested \$250,000 into the business, the capital gain would be \$750,000 with the result that tax would be payable on \$375,000 and the other \$375,000 would be tax free.

This may sound good (in particular, the "tax free" part), but if you don't have the cash, where do you get the money to pay the tax on the \$375,000 given that the farming operations have not been sold, but only deemed to have been sold by tax law.

The answer is in more tax law. If you have a spouse, you are allowed to transfer your farming operations to your spouse on a tax free basis. This is known as a "tax-free rollover" which allows the payment of the tax to be deferred until your spouse sells the farming operations or your spouse's death. As well, if you hold your farming operations in a family farm partnership or corporation, there are also a series of complicated situations where you may transfer the interest to your spouse or child on a tax free basis. For these situations, you are best advised to consult your tax advisor.

The tax law also permits some post-death tax planning to take place. For example, at the time of your death, if you have unused capital losses, you will want to have a capital gain to off-set the losses. In this case, your legal representative is allowed to deem the transfer of the farming operations at an amount somewhere between the fair market value and your cost base of the operations, which allows the capital loss to be used up and the reduced capital gain to be deferred.

So even if you do not have a plan, the tax law will provide reasonable options to allow you to defer tax. But a succession plan is much more than tax planning, so invest the time to meet with your advisor, whether it is an accountant, a lawyer, or both, to plan the succession of your farming operations. Your family will appreciate it.

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