Hanging on or handing over: proceedings of a Succession Planning Seminar held ... 28 July, 1994 at the Dalwallinu Recreation Centre ... 29 July 1994 at the Moora Recreation Centre.

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Succession Planning Seminar

"Hanging on or handing over"

Proceedings of a Succession Planning Seminar held:

Thursday, 28 July 1994 at the Dalwallinu Recreation Centre
Friday, 29 July 1994 at the Moora Recreation Centre

Sponsors of the day are gratefully acknowledged:

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INTRODUCTION

Sonya Butt, Regional Economist, Department of Agriculture, Moora

The two inevitables of life are death and taxes and never has there been a more direct application to these inevitables than the old Russian proverb-

"If you fail to plan, you are planning to fail."

In 1980 in the Shires of the West Midlands and Northern Wheatbelt there were 1,102 farm enterprises. By 1993, there were 853 farm enterprises - a decline of 23% and one of the major factors causing this decline is the lack of effective estate planning. It confirms that a significant proportion of farm businesses do not have the resources to fund the retirement of parents and leave a viable business for the younger generation to inherit.

If the second generation is to successfully take over the family farm it is far more likely to be achieved following careful planning, rather than sudden retirement, illness or death being the pivot around which younger farmers get thrown in at the deep end.

The speakers at today's seminar have been organised in their respective fields to help you better understand the related issues of succession planning working towards sustaining the farm family unit. It is hoped at the end of the seminar you will be better able to go about starting your own plan that will suit your requirements.

These proceedings have been written by the speakers today and the time and effort of the authors is greatly appreciated. Thank you also to R.A.F.C.O.R. for providing sponsorship towards the cost of this seminar.
WHAT CAN A RURAL COUNSELLOR OFFER?

Peter Fisher, Rural Counsellor, Moora

INTRODUCTION

1. A general overview of the succession planning process.
2. Assistance in drawing up an estate plan.
3. Mediation counselling to resolve inter family conflict arising out of the proposed plan.

1. A general overview of the succession planning process.
   1.1 An outline of the types of options available.
   1.2 Information on sources of professional expertise.
   1.3 Discussion on alternative retirement income sources, e.g. Aged Pension.

2. Assistance in drawing up the estate plan.
   2.1 Balance sheet analysis to determine who owns which assets and which assets are subject to finance house securities.
   2.2 Clarify the testators wishes as to which beneficiaries will inherit which assets.
   2.3 Options on ways in which the assets may be transferred without having a detrimental effect on the continuity of the family business.

3. Mediation to resolve inter family conflict arising out of the proposed succession plan.
   3.1 Interview individual family members to gain an overview of the personal goals and aspirations of each.
   3.2 Analyse the information gained in order to present ways in which the conflict may be resolved.
   3.3 Provide a written report to the principal asset holder setting out findings and possible solutions.

CONCLUSION

The purpose of rural counselling is to enable farming families to effectively assess the options available to them, and to use the information gained to make informed decisions about the future direction of both the family business and those relying upon it as their source of income.
HANGING ON OR HANDING OVER THE FAMILY FARM

Graeme Thygesen, Bird Cameron Chartered Accountants, Perth

INTRODUCTION

Most farms in Australia are family farms. These can vary from sole traders to husband and wife partnerships to large complex structures that can cover many generations of farming families.

While succession planning involves the transferring of farming assets from one generation to the next, at the same time ensuring financial security for the parents and financial viability for the farm, the most important aspect of succession planning is people. This is especially so in farming.

Due to the individual nature of succession planning, it often puts a strain on existing family relationships and structures. Unfortunately, there is no universal panacea that will solve every family situation. However, in any given situation, communication, long term planning and education will help.

CONCERNS OF THE FIRST GENERATION

Many people fail to plan for business succession and farmers are no different in this regard. Where they are different however is that their livelihood has depended upon farming assets (land, machinery and livestock) which they should transfer to their farming children.

Below listed are some of the reasons given by the first generation for not transferring the farming assets to the second generation. They are either real or perceived problems but usually are not of sufficient concern to prevent the transfer of farming assets. The problem has been given to be:

Fear of creating family conflict once their intentions are known.

The desire to be fair to all their children but at the same time pass on a viable farm to the farming generation.

Waiting to see how things eventually work out between their children's career and the farm.

The cost of transferring farming assets, especially stamp duty.

Fear that divorce of a second generation member will cripple the farm.

The fear that they may no longer be a useful contributor to the farm and have nothing to do.

Lack of housing as their home is on the farm and they feel that if they transfer the farming property they are obligated to leave.

Not having sufficient funds to provide an adequate retirement income.

The fear that the children may sell the farm, once transferred.
The University of Western Sydney conducted a survey amongst first and second generation farmers to record the concerns of the first generation in transferring farming assets. The table below is a result of their survey.

Table 1: The level of farm transfer concerns of the first generation farmers on 1st and 2nd generational family farms.

<table>
<thead>
<tr>
<th>Concerns</th>
<th>Average Score on 2nd Generation Farms</th>
<th>Average Score on 1st Generation Farms</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. To treat all my children fairly.</td>
<td>3.9</td>
<td>3.7</td>
</tr>
<tr>
<td>2. To ensure financial security to my child or children taking over the family farm (e.g. keep the farm in the family name).</td>
<td>3.6</td>
<td>3.0</td>
</tr>
<tr>
<td>3. To establish one or more of my children in farming.</td>
<td>3.4</td>
<td>2.4</td>
</tr>
<tr>
<td>4. To ensure financial security for myself.</td>
<td>3.3</td>
<td>3.1</td>
</tr>
<tr>
<td>5. The possible loss of our farm through divorce in the younger generation.</td>
<td>3.1</td>
<td>2.6</td>
</tr>
</tbody>
</table>

NOTE: A score of 1.0 is extremely unimportant. A score of 4.0 is extremely important.

The concerns listed above highlight some of the important issues when transferring farming assets between the first and second generations. It may be noted that the above table recognises a desire to treat all children fairly, however, there is recognition that to pass a viable farming unit, could well mean the exclusion of some children over others.

CONCERNS OF THE SECOND GENERATION

The second generation members have their own concerns, the main being when to commence discussions with their parents regarding the transfer of farming assets. One of the major impediments to second generations taking the initiative to commence discussions of transferring the farming assets is that they are usually dependent on the first generation for their livelihood, occupation and future.

There is a perceived resistance by the second generation to initiate the discussion with the first generation regarding the transfer of farming land. They feel that it is the first generation’s place to commence discussions on the transfer as it is their assets which will be transferred.
Table 2: Summary of the concerns of married second generation farming men and women.

<table>
<thead>
<tr>
<th>Concerns</th>
<th>Average Score</th>
<th>Average Score</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>For Farming Men</td>
<td>For Farming Women</td>
</tr>
<tr>
<td>1 To be involved in any decision making regarding the</td>
<td>3.19</td>
<td>3.27</td>
</tr>
<tr>
<td>future of the family farm and my parents intentions for</td>
<td></td>
<td></td>
</tr>
<tr>
<td>each of their children.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2 To not have to guess what the intentions of my parents</td>
<td>3.05</td>
<td>3.48</td>
</tr>
<tr>
<td>are in relation to me and my brothers and sisters, e.g.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>what is in their Will.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>3 To be included in the business structure, e.g. partnership</td>
<td>2.91</td>
<td>3.24</td>
</tr>
<tr>
<td>4 To be given management responsibility as soon as possible.</td>
<td>2.73</td>
<td>2.96</td>
</tr>
<tr>
<td>5 To be given ownership of the farm</td>
<td>2.52</td>
<td>2.57</td>
</tr>
</tbody>
</table>

NOTE: A score of 1.0 was extremely unimportant. A score of 4.0 was extremely important.

As can be seen from the above table, the major concern for the second generation families is to be involved in the decision making process which involves the family farm and their future. Another pressing concern for many is to be included in the family partnership or business structure to have a sense of belonging and to be able to contribute to the family farm. Also of interest is that the women have a higher concern level in every area over men.

COMMUNICATION

As mentioned earlier, the second generation’s inability to discuss openly with their parents, matters concerning the transfer of farming assets will lead to tension within the family unit.

Table 3: Summary of the mode of communication for first and second generation participants on two generational family farms (1).

<table>
<thead>
<tr>
<th>Concerns</th>
<th>Average Score for First Generation</th>
<th>Average Score for Second Generation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1 One to one.</td>
<td>2.5</td>
<td>2.2</td>
</tr>
<tr>
<td>2 As a whole family.</td>
<td>2.4</td>
<td>1.8</td>
</tr>
<tr>
<td>3 Parents initiating discussion with returning children.</td>
<td>2.3</td>
<td>1.9</td>
</tr>
<tr>
<td>4 Returning children initiating discussion with parents.</td>
<td>1.8</td>
<td>1.8</td>
</tr>
<tr>
<td>5 As a whole family with a professional adviser.</td>
<td>1.6</td>
<td>1.5</td>
</tr>
</tbody>
</table>

NOTE: 1-Never 2-Sometimes 3-Fairly often 4-Very often
Table 3 indicates a very low level of discussions occurring between family members. There is a strong indication that there is a difference between perceived communication between the first generation and the second generation regarding the transfer of farming assets. The above table indicates that parents consider that they talk more with their children regarding the transfer than their children perceive to be the case.

This has been brought out by a recent 1991/92 study of New South Wales farming families which reveal that:

- 42% of parents did not discuss the subject of inter generational transfer with each other.
- 63% of parents had not spoken to the second generation about transferring of the farm business.
- 84% of the parents had not included their daughter-in-law in any discussions, even though it had a major effect on her life and family.

The level and openness of communication within families will of course differ from family to family. Overseas studies have shown where two generation farm families talk openly about farm transfer on an on-going basis in terms of their needs, desires and future aspirations, they are more likely to survive the transition with minimum stress and keep the farm in the family for another generation.

The same study has also shown that families with a more open communication style and more open decision making will have significantly less stress during the process of transferring the family farm.

Conversely, in families where the level of discussions between family members for transferring of family farms is not as open, the level of stress is significantly greater. This leads to a concern in the second generation as regards to not only their own ability but also their future livelihood and future on the farm.

One of the most common methods of transferring farming assets to a second generation are via the Wills of parents. Transferring the family farm via the use of Wills is usually not a problem where there are open discussions on succession within the family.

As indicated in Table 2, not knowing how the parents are to transfer the family assets in their Wills is a major concern for the second generation families.

A recent study conducted in rural New South Wales and Queensland revealed that 8% of first generation farmers did not have a Will. Furthermore, 55% of the children did not know what their intentions were in relation to transferring of the farming assets. This clear breakdown in communication between the first and second generation is a major source of concern and stress for the second generation.

**PLAN FOR THE FUTURE**

The best plans for a family succession should start with the mother's and father's retirement plans and work backwards through the steps you will take to get there on time. These plans should be discussed openly with the farming children so that they can see where they are going and what
they are working towards. Such plans can develop their personal skills so that they are equipped to take over each particular stage. These can include outside experience and farm management education. Where there is no plan or no communication of the plan between the parents and the next generation, this leads to conflict within the family and the family pulled in different directions and not having a common purpose to work towards.

There are several important areas where a plan is needed.

A work plan - what everybody will be doing and when. The family, farm workers and contractors included. Make the best use of each individual's abilities.

A production plan - how much wheat we will grow this year, sheep we will run, machines we will buy and so on.

A business plan - which looks at capital growths (on and off the farm) and monitors your equity position.

A financial plan or budget based on the plan. This will show where the money is coming from and what it is being used for. It is a communication tool for the family members and financiers.

An estate plan - which includes Wills, partnerships, trusts or whatever to minimise tax and meet personal objectives. It will include a definite date for handing over areas of management and decision making.

Self-development plans. This includes things as what skills the staff or boys need, where they will be acquiring them and when. It might include some refresher schools for Dad in estate planning or the like.

Plans can be changed with good reason, but at least you know what you are changing. Where you can't create this sort of environment, the assistance of professional advisers should be sought.

By use of these plans, some of the concerns mentioned previously by the first generation can be diminished as all the areas that were of concern to them have been properly planned and worked out to ensure a smooth transfer of the farming assets. Where the farm can support only one family, some retirees hope to live on the age pension, but giving away the farm does not ensure immediate eligibility. To ensure eligibility for the age pension a gradual and planned disposal of assets is required to be completed five years prior to the receipt of an age pension to ensure the eligibility of that pension under the asset test.

**WILLS AS A PART OF YOUR SUCCESSION PLAN**

As mentioned earlier, a common method of transferring farming assets are via the Wills of the parents. This is because we cannot be sure that we have disposed of our assets during our own lifetime.

Most of us should probably revise our Wills at least every five years, because one of the following events is likely to occur within that time:

Marriage.
Divorce.

Death of an executor or beneficiary.

Birth of children.

Change of wealth.

The major problem in transferring farming assets this way is the average life expectancy of males and females if between 75 and 80 years of age. This means that by the time the farming children receive their inheritance, they may well be in their mid-fifties. At this stage, their own succession plans should be well advanced.

To avoid the uncertainties and the associated stress that the second generation will experience in not knowing their future, farming assets should be transferred during the life of the first generation. However, the need to ensure the first generation has sufficient security after transferring the asset should be paramount at all times.

The State Government has recently announced that legislation will be placed before the house in December this year to ensure that stamp duty on transfer of farming assets within the family will be exempt from stamp duty. It is unclear at this stage to what extent such an exemption will cover however, we are waiting on the legislation with much interest. We anticipate that the legislation will be in line with the Victorian legislation which is fairly wide and will enable most family transfers of farming assets to be dealt with. This gives an excellent opportunity to start implementing family succession plans which in the past have been delayed due to the cost of stamp duty which would have been involved on the transfer of the farming assets.

EDUCATION AND SELF-DEVELOPMENT

As mentioned before, self-development plans will enable you to ascertain what skills are required by the family to ensure the transfer of the farm management can be undertaken from one generation to the next. Education can help in two ways to ensure a smooth planning and other facets of retirement. This will increase the level of knowledge (particularly with the first generation) on this matter.
1. GENERAL PRINCIPLES OF TRUSTS

Trusts is a division of ownership of property where a trustee holds the legal interest in the property and a beneficiary holds the beneficial interest. The most common form of trust is an estate where a person dies and an executor is appointed as trustee to hold the legal interest in the property for ultimate division and transfer to the persons entitled to the property pursuant to the provisions of the Will and these people are called the beneficiaries.

A Discretionary Family Trust is a special type of trust where a trustee has a discretion in regard to the following matters:

(a) The date upon which the trust property is transferred to beneficiaries.
(b) To which of the beneficiaries the income is distributed.
(c) To which of the beneficiaries the capital is distributed.

2. THE DISCRETIONARY FAMILY TRUST

The person who creates the trust is called the settlor and must not play any further role in the trust other than the creation of the trust with a nominal sum of money and setting the terms of the trust deed.

A trustee is appointed by the trust for the purpose of holding all of the trust assets upon the terms and conditions set out in the trust deed. This can either be an individual or individuals or a proprietary limited company.

Property is either then gifted into the trust or acquired by the trust and then held by the trustee upon the terms and conditions of the trust. The trustee must not mix the trust property with its own property. Separate accounts must be kept for the trust assets.

The beneficiaries of the trust are generally divided into two classes:

(a) The primary beneficiaries or capital beneficiaries are specifically named persons who will take the trust assets of the trustee exercising his discretion.
(b) The general beneficiaries is usually a very wide class including all lineal descendants of the controllers of the trust together with associated trusts and companies and any charitable institutions.

The guardian and appointor are the persons who have effective control of the trust and the trustee can generally only exercise the discretions or amend the trust deed with the consent of the guardian and appointor. Provision must be made for a succeeding guardian and appointor upon the death of the named guardian and appointor to give continuity to the capacity to exercise the discretion.
Often infants or juniors are introduced into the partnership for “taxation purposes” but do not undertake the normal partnership work and conversely when members of the partnership have retired they continue to remain a member of the partnership not withstanding that they are no longer active in the partnership business. We strongly recommend that only active members of a partnership are members of the partnership and other methods are used for taxation minimisation and for payment to retiring persons after they have retired.

In a law practice you would not entertain having a partner who does not work full time in the partnership.

Having partners continuing in a partnership when they are no longer making an active contribution distorts the capital accounts and in the event of a later dispute the distorted capital accounts can cause considerable difficulties in regard to a disputed dissolution of partnership.

Partnerships are governed by the Partnership Act which is comprehensive in setting out the relationship between the parties. A written agreement is not necessary and a partnership can arise by a course of conduct. A registered business name is necessary and compulsory where a name is used other than the names of the partners.

A written Partnership Agreement should be entered into as it compels the partners to address various issues of carrying on business together in partnership which are summarised as follows:

1. Limiting the amount a partner can pledge in credit or in a purchase of partnership equipment without a unanimous partnership decision.
3. Death of a partner.
4. Break down of marriage between two members of the partnership.
5. Pay out of retiring partners.

The preparation of the Agreement is an essential part of the communication in family business that should take place. There should be a plan developed involving the members of the farming business and the professional advisers including accountants, consultants and solicitors as it is imperative that the best structure is developed both from a taxation point of view and from the family relationships point of view and then continued review and change and planning is made.

Upon a son who is a partner entering into marriage the situation of the family has changed and consideration should then be given. We often find that daughters-in-law coming in to farming partnerships cause a stress and it is generally preferable to introduce a trust into the partnership as the additional partner of which the daughter-in-law is a beneficiary. Income can then be distributed but control over the partnership, its assets and its members are still retained within the family.

We have already dealt with Trusts and the control that Trusts give over the particular operation.
CORPORATIONS

1. Corporations are governed by the Corporations Law and have been developed through legislation rather than through the common law which has developed the concepts of Trust and Partnerships. A company only exists through statute law and is extensively controlled through the Corporations Law which has moved from fragmented state by State legislation to standard Australia wide legislation.

2. Companies are rigidly controlled by the Corporations Law and the controls on companies and their governing officers is continually being extended.

3. A company is a separate legal entity with the capacity to enter into contracts and to sue or be sued and is a tax payer in its own right. This is opposed to a Trust which is not treated as a separate entity for taxation purposes. Similarly, a Partnership is not taxed as a partnership.

4. A company enjoys a flat rate of taxation over all of the net income of the company and due to this rate presently being considerably below the marginal rate of taxation for individuals, there has been a rush by persons on high incomes to operate through a corporation to take advantage of the lower tax rate.

5. Companies are often used as land holding vehicles and were often set up during the 1950's and '60's to hold land with governing director shares that had a very small ownership of the total shares on issue. This was to enable a person to control the company but on his death would have very little assets in his own name for estate and death duty purposes.

6. A company is a rigid vehicle and once shares have been issued, the shareholder has rights to make certain the company is properly administered and the shareholding is not diluted by the issue of further shares without that shareholder's approval. Land owning companies are often difficult to take into consideration in the transfer of assets as shares have often been issued to various members of the family who are not farming and unless the shareholders voluntarily agree to transfer the shares, the shareholder will continue to own shares in the company that owns the land. A company does not have the flexibility and discretions that are available through a family trust.

7. Often a family trust will have a corporate trustee. This means that instead of having individuals as the trustee, a company is specially incorporated for the purpose of being the Trustee of the family trust. The trustee does not own any assets in its own right but only owns the assets for and on behalf of the trust. The corporation as trustee lodges a tax return in its own right and a tax return on behalf of the trust. The tax return in the trustee's own right shows that it earns no income and only has $2.00 in assets. The second return that is lodged is lodged by the company as trustee on behalf of the family trust.

8. A company is controlled by the shareholders who elect a board of directors who then have the on-going management control of the company. The Corporations Law provides extensive obligations and responsibilities to directors of a company and, in particular, the directors must not carry on the business of the company when they become aware that the company may not be able to pay the liabilities of the company as and when they fall due. A breach may mean the directors are personally liable for the liabilities of the company and in addition may face penal process from the Australian Securities Commission.
3. GENERAL FEATURES OF THE DISCRETIONARY FAMILY TRUST
SEPARATE LEGAL ENTITY

The trust is a separate legal entity and separate accounts must be kept and separate records of the trust must be kept. The initial settled sum which is generally in the vicinity of $100 needs to be paid into a separate bank account owned by the trust.

The trust then accumulates assets by acquisition of gift and these are reflected in the balance sheet. Controllers of the trust need to give special attention to the loan accounts between the beneficiaries and the trust as loan accounts can rapidly build up with distributions of profit and capital that are not applied by way of cash. In the event of the insolvency of a beneficiary or principle of the trust the loan accounts of the trust are very closely examined by the trustee in insolvency. It is important to endeavour to keep the loan accounts to a minimum level.

4. CONTINUITY OF THE TRUST

It is important that the controller of the trust gives consideration to who will be exercising the discretions as to the distribution of income and capital and the ultimate winding up of the trust after his death. The trust often holds more of the assets of the controller than in his own name and the trust document and its continuity becomes more important than the Will. The guardian and appointor will need to make certain that a person whom he closely trusts is appointed to the position of guardian and appointor on his death with some direction as to how the previous controller wishes the discretion to be exercised.

5. THE BENEFICIARIES

The beneficiaries do not have any legal interest in the assets of the trust. The only interest that they have is in regard to loan accounts after there has been an application of trust income or trust assets in their favour. Prior to the exercising of the discretion in their favour the general beneficiaries can only describe their interest as a contingent expectant interest. They cannot force the trustee to exercise the discretion in their favour and the discretion when exercised can only be attacked if reasons for the exercise of the discretion are given by the trustee and the reasons are found to be unreasonable. It is therefore important that on any distribution of income or capital by the Trustee no reasons for the distribution are given.

6. INCOME DISTRIBUTION

It is important that the income of the trust is distributed by trustee minute prior to the end of the financial year in each year. Income of the trust that is not distributed will attract tax at the higher rate. It is therefore important that careful consideration is given to the distribution of income to the best taxation advantage between the beneficiaries. However, considerations other than income tax will also be taken into effect as once the distribution is made by the trustee of income it becomes a debt owing by the trustee to the beneficiary and the beneficiary can demand payment of the debt as with any other debt.
7. VESTING OF THE TRUST

The trust deed generally allows the trust to operate for the maximum period of eighty years with a discretion in the trust deed to bring the date forward. It is important that the continuity of the positions of guardian and appointor is provided for as in the event of there being a guardian and appointor the trust deed does not have a capacity to bring forward the vesting date and the trust must then run the full period of eighty years.

On the vesting day the trustee with the guardians consent may distribute the income and capital of the trust to any one or more of the beneficiaries in such proportions as the trustee at its discretion shall decide. If the trustee does not exercise its discretion in regard to the distribution of capital on vesting then the primary beneficiaries of the trust will be entitled in equal shares.

PARTNERSHIPS

Partnerships are probably the most common form of business relationships. A partnership can arise by a course of conduct or by a calculated decision.

The legal definition of a partnership is as follows:

Two or more persons carrying on business together in common with a view to profit.

Going into partnership with a person requires detailed and careful consideration and planning prior to the commencement of the partnership. We are very critical of persons being introduced into the farming partnership for “taxation purposes”.

We believe that there is much more to a partnership than the taxation advantages and detailed discussion should take place between the continuing partners and incoming partner prior to the introduction of the new partner clearly setting out the aims and objects of the partnership and the role of each member of the partnership in carrying on the partnership business.

The main disadvantage of a partnership is the unlimited liability of the members of the partnership for the debts of the partnership. Any one partner can incur the credit of the partnership and bind other members of the partnership to all of the liabilities incurred.

A partnership is based upon the law of trust. Not only upon the law of trust but on the generally accepted concept of the use of the word trust, it is important that all members of the partnership have the absolute trust and confidence of the other members of the partnership or the relationship will break down.

Partnership disputes are probably the most difficult area of law and often emotions in a partnership dispute cause the dispute to be likened to a matrimonial break down where it is very difficult for reasoned and objective decisions to be made.

A method needs to be developed with partnerships for a transition of ownership and we generally recommend that only working partners are members of the partnership unless some other arrangement is entered into to reward the partners who are carrying on the partnership business.
WILLS AND THE INHERITANCE (TESTATORS FAMILY MAINTENANCE) LEGISLATION

1. On the death of a person, the Estate must be administered. It is an advantage if the person prepares a detailed Will to provide for the appointment of an Executor to administer the Estate and then gives clear, precise instructions to the Executor as to the disposal of the various assets that are owned by the Testator. The Will should be updated at least every five years, taking into consideration the following:

(a) the Executor needs to be somebody who understands the business aspects, is absolutely trusted and understands the position of the Beneficiaries and the family.

(b) a detailed list of assets should be prepared and considered.

(c) the position of all potential Beneficiaries should be considered and, in particular, the spouse and all children and their interests must be considered.

2. If a person dies without a Will, they die intestate and the Administration Act provides that the nearest next of kin can apply for Letter of Administration to administer the Estate or if no member of the family wishes to apply, a creditor can apply.

The distribution of the assets is set pursuant to the Administration Act which provides rigid rules dependant upon the level of the Estate.

3. The Will becomes an operative document from the date of death. The Will may be executed on the 1st day of July 1985 and Testator dies on the 1st day of July 1994 and date of operation of the Will is therefore the 1st day of July 1994, not withstanding that it was signed some nine years earlier. It is very important to consider the nature and changing nature of your assets and your family when you are preparing a Will. The Will may come into existence some considerable time after it is signed.

4. The powers of the Executor as a Trustee are derived from the Trustee’s Act and any other powers which you wish to give to him pursuant to the terms of the Will. You may wish to give the Trustee more extensive powers to deal with farming property, to enter into Sharefarming Agreements and Lease Agreements, to mortgage the property and all other extensive powers so that the farming operations can be carried on.

5. The Courts are becoming increasingly concerned to interfere with Wills where it is considered that the Testator has not made adequate and proper provision for his family and dependants. No longer can a person who controls assets in his own name leave all of the assets to a son and leave the other members of the family without significant benefit under the Will. The Courts will use the provisions of the Inheritance (Family and Dependants) legislation to basically re-write the Will.

The Courts are always reluctant to interfere with a person’s testamentary intentions but there is an increasing trend to use the legislation to provide for equity between the members of the family. When Court cases commence in this area, significant evidence is required as to the contributions and the needs of the various members of the family and there is no clear cut or rigid rule in regard to the distribution. It would depend on the
quality of the case presented to the Court and the attitude and intention of the Judge in regard to re-writing of the Will to provide for equity between the members of the family.

It is now very important to consider the provisions of the whole of the family when preparing the Will and to make reasonable and fair provision for the children who are not going to inherit the significant part of the farm assets.

6. Every possession is different and every farm set up has a different legal and business structure and a different family structure and it is important that you always give consideration to this section of the law and that you obtain proper legal advice in regard to preparation of the Will.

7. We believe that it is important that in regard to preparation of the Will, that all of your consultants and advisers are involved and not merely the solicitors. Due to the complexities of business in modern day farming, a normal farm will generally have a company, a trust, a partnership and a sole trader with off-farm investments in various different names and maybe a self-managed superannuation fund. It is difficult for a solicitor to fully understand the relationship between all of the entities and we believe that it is important to have the input of your accountant and your farm adviser in regard to the balancing of the interest between all of the family and all of the assets in the preparation of the Will.

9. The Inheritance legislation does not apply in regard to assets that are not owned by you but are owned by separate entities such as a trust.
UNDERSTANDING YOUR PRESENT STRUCTURE

Tony Barber, Bird Cameron Chartered Accountants, Moora

TYPES OF TRADING ENTITIES

Sole Trader

Partnership

<table>
<thead>
<tr>
<th>Trust</th>
<th>Company</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Discretionary Trust</td>
<td>- Ordinary Company</td>
</tr>
<tr>
<td>- Unit Trust</td>
<td>- Trading Company</td>
</tr>
<tr>
<td>- Class Trust</td>
<td>- Land or Asset Owning Company</td>
</tr>
<tr>
<td>- Trading Trust</td>
<td>- Partner Company</td>
</tr>
<tr>
<td>- Land or Asset Owning Trust</td>
<td>- Trustee Company</td>
</tr>
<tr>
<td></td>
<td>- Beneficiary Company</td>
</tr>
</tbody>
</table>

THE USES OF DIFFERENT TRADING STRUCTURES

I often use Ralph Sarich as an illustration to show the different trading structures that businesses use. (I have no idea if Ralph actually progressed like this by the way).

- Ralph probably started as a mechanic with GMH - on wages.

- Perhaps he then decided to work in his own shed, and he would have then operated as a sole trader, i.e. Ralph Arthur Sarich.

- If he worked hard with a reasonable income, his accountant would have recommended that he bring his wife into the partnership. (This is assuming his wife had no other income, and that splitting the income was useful), i.e. R. A. & B. E. Sarich.

- If he continued to expand, he may have brought other people, i.e. family, other mechanics etc., into the business, perhaps first as employees, then as partners, i.e. R. A. & B. E. Sarich & Partners.

- At some point he may have converted his business to a trading trust. This would have given a couple of advantages:
  - he would have been in control
  - he would have saved accountancy and bank fees everytime someone came in or went out of the business
  - he could have paid himself and his wife wages
- saving provisional tax, but paying Pay As You Earn Tax
- paying worker's compensation insurance
- there may have been superannuation advantages
- there would have been flexibility in allocating income between people, i.e. working and non-working people, children under and over 18 etc.
- since companies at the moment have a flat rate of tax of 33%, if the individual's tax rate is over that, then it is attractive to have a company as beneficiary and have it pay tax
- a trading trust for legal reasons, usually has a company as trustee (called a corporate trustee). The trade name would then be something like - Sarich Pty. Ltd., as trustee for the Sarich Family Trust, trading as R. A. & B. E. Sarich & Partners. (Pty. means proprietary, and this refers to it being a "private" company. Ltd. means limited, and refers to liability. If the company goes broke, the shareholders are not responsible, unless they have signed a directors guarantee).

- At some further point Ralph would have wanted to work less and concentrate more on his inventions. He would have probably initially perhaps borrowed from friends and family, then the bank, to finance this. As the need for finance became greater, he would have run out of places to borrow and decided to go to the general public for funds. He would have probably formed another company, say Orbital Ltd., and "floated" the company through the stock exchange. The public put money in, and in return, owned a part of the company, i.e. shares. You will notice that this company is called "Ltd.", not "Pty. Ltd.", and that is because it is a public, not a private company. It is still Ltd. as far as liability goes, i.e. if Orbital goes broke, the shareholders lose their investment, but cannot be asked for any further money.

PARTNERSHIPS

- The most common form of business structure is a partnership. Peter Michael has already outlined the legal aspects of partnerships.

- The partnership usually owns the livestock, plant and machinery, CBH tolls and trading account, and the debts of the business are usually shown as partnership debts, e.g. overdraft, term loan, stock firm and hire purchase.

- Partnerships are reasonably flexible in the allocations of income, and this is done by partners salary. In a four way partnership, if one partner is working off the farm, we would allocate the profit to the other three partners. It is not advisable to do this in the long term as the salaries need to be reasonable.

- We get a lot of queries about partnership equities. This is almost a loan account that each partner has with the partnership. As the farm makes a profit each year, each partners' share is credited to their loan or equity account. As each partner draws money during the year, this amount is debited to their equity account (this may be their share of personal drawings, taxation, a car etc.). Usually "Dads" equity is the highest as he probably started the farm or inherited it, but it would be the same if the assets had come from "Mum". In fact I have had cases where daughter-in-laws have contributed money, and their equities reflect this. It is
common for land to be purchased in say the son's name, and this would be debited to their equity account. Many may have a large deficiency because of this. Parents equity would also be reduced with the purchase of a retirement house, off-farm investments or superannuation contributions. People often worry about one brother who has five children at boarding school, whilst another brother is unmarried. In that case, the equity of the brother with the five children would have the education costs taken off each year. Over time, his equity would be considerably less than this brother.

- Partnership Variations also cause a lot of confusion. It is important to be aware that if for instance "Mum" and "Dad" being "Son" into the partnership, that he is not automatically entitled to one-third, but he effectively owes his parents for that one-third value. I have written this out to illustrate how it would appear on the partnership books.

### ASSETS OF PARTNERSHIP

<table>
<thead>
<tr>
<th></th>
<th>At book value</th>
<th>Before Son Admitted</th>
<th>After Son Admitted</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Asset revaluation</td>
<td>Market value</td>
<td>Asset devaluation</td>
</tr>
<tr>
<td>Cash</td>
<td>50,000</td>
<td>-</td>
<td>50,000</td>
</tr>
<tr>
<td>Machinery</td>
<td>130,000</td>
<td>70,000</td>
<td>200,000</td>
</tr>
<tr>
<td>Livestock</td>
<td>20,000</td>
<td>30,000</td>
<td>20,000</td>
</tr>
<tr>
<td>Total</td>
<td>200,000</td>
<td>100,000</td>
<td>100,000</td>
</tr>
</tbody>
</table>

### EQUITIES

<p>| | | | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Dad</td>
<td>130,000</td>
<td>50,000</td>
<td>180,000</td>
<td>(33,334)</td>
</tr>
<tr>
<td>Mum</td>
<td>70,000</td>
<td>50,000</td>
<td>120,000</td>
<td>(33,333)</td>
</tr>
<tr>
<td>Son</td>
<td></td>
<td></td>
<td></td>
<td>(33,333)</td>
</tr>
<tr>
<td>Total</td>
<td>200,000</td>
<td>100,000</td>
<td>100,000</td>
<td>200,000</td>
</tr>
</tbody>
</table>

### TRUSTS

- Unit Trusts and Class Trusts are not common, so I will not spend time on those.

- Farmers mainly have two uses for trusts, either a trading trust in its own right, or as a partner, and as a landowner. The uses of a trading trust I have outlined briefly in the Ralph Sarich example, but the other main use is as the owner of the land. In the past we have had probate, stamp duty on land transfers, assets tests for pensions and education allowances and possible capital gains tax on land transfers and bank costs to transfer mortgages. We set a lot of trusts up in the seventies to buy the land from the family members, and we would pay rent to the trust, and allocate the income to the children in the family. (Children in those days could receive income to the equivalent adult tax threshold with nil or low rates of tax. We cannot do that now as children pay penalty rates up to age 18 on income over $416). Probate was minimised because "Mum and Dad" did not own the land (although as trustees they controlled it), and when assets tests on age pensions and education allowances came in there was a real bonus as again "Mum and Dad" did not own the land.
Stamp duty on transfers between generations did not have to be incurred, and when capital gains tax was introduced in 1985, this too was not incurred. Michael Pedley will talk on Capital Gains Tax and security of parents as well as pension implications shortly.

- If you currently have a land owning trust, they are still useful for transition of ownership because the transfer of land will still involve costs such as:
  - legal and conveyancing costs
  - bank costs to transfer mortgages
  - possible capital gains
  - loss of security to parents

COMPANIES

- Many of you would have a company or two. Some of these may date back to the sixties when companies were set up to own land. This was to avoid land being in individual's names which would then be subject to death duties when the owner died. Usually one or two shares were in the parents' names (Governing Director shares), the rest in the children's names. The use of these companies was phased out and replaced by trusts in the seventies. Many of these companies have shareholdings that may not be appropriate for you today. There is a cost to liquidate these companies and pass the land to the shareholders (care needs to be taken to make sure the shares are owned by the right people, and trusts as shareholders may be useful). This cost needs to be weighed against the cost of continuing to own the companies, which involves accountancy and Australian Securities Commission fees each year. We do sometimes use these companies to take advantage of the company tax rate of 33% (usually by paying rent).

- Most newer companies will be either:
  - Trustee Companies - these act as trustee of a trust
  - Beneficiary Companies - these act as beneficiaries of a trust to take advantage of the company tax rate of 33%
  - Partner Companies - although not common, a company may be introduced into the partnership to take advantage of the company tax rate of 33%.

OWNERSHIP OF ASSETS

- Step one in working out each person's value of any business is to work out who owns what. We call this (in our firm) a wealth appraisal statement. It involves the companies, trusts, partnerships and individual holdings and puts them in a way to see who is the actual owners, and what the value of each owner is.

- Once the assets and values are known, we would then sit down and discuss the results with the family. If a trust or company is involved, much of the value of the assets may already be in the children's names, however it may be the wrong children. "Mum" and "Dads" Wills may
refer to an asset they may not actually own. There may be an amount on an old contract of
sale that should have been finalised years ago. The non-farming children may have loan
accounts with the trust from distributions allocated in previous years. Perhaps a third
generation is now involved with the farm. Perhaps land could be transferred to a trust rather
than held in an elderly person's name. Farming assets should be separated from non-farming
assets.

- The Wills should then be reviewed to see that they tie in with what is the situation now, and
what it is desired to be. Farming assets need to be clearly identified, e.g. are Wesfarmers
shares farming or non-farming assets? If shares are held jointly with other people, can they be
disposed of in their Will, or do they go automatically on death to the other joint owners?
Capital Gains Tax (CGT) may apply if you sold or disposed of assets purchased or deemed to have been purchased since 19 September 1985.

Excluded assets include certain motor vehicles and motor cycles, trading stock and a tax payer's principle residence. Capital gains are indexed if owned for more than a year, and capital losses can occur but broadly speaking only useful to off-set against gains.

The initial choice of a structure should be carefully considered because changing a structure mid-stream could cause CGT problems. It should be noted however that rollover relief provisions do exist and should be explored. Similarly planning should be made so that assets retain their pre-September 1985 status. For example partnerships that expect to introduce or remove partners on a regular basis should not own assets subject to capital gains.

Averaging concessions apply when individuals receive capital gains. Averaging is achieved by determining the amount of tax payable on one-fifth of the gain at an individual's rate and multiplying the gain by five. This can mean that an individual with no other income can receive up to $27,000 capital gain before paying tax, taking advantage of the $5,400 tax free threshold.

When deciding on a structure Capital Gains Tax should be considered, in many situations, elections, market valuations, rollover relief provision or simply the timing of disposals can alter capital gains liabilities.

**ELIGIBILITY FOR OLD AGE PENSION**

In many situations and especially with the expected transfer of farms from one generation to the next, many in the 50+ age group will need to consider their options. For many, the old age pension will be an option. With the "Parents" receiving a pension, a degree of financial pressure will also be removed from the family business.

To achieve eligibility for pension a gifting of assets may need to take place. Currently under the 'assets test' a married couple may have up to $160,500 worth of assets, excluding home (single up to $112,750). Under the 'income test' a married couple may earn up to $1,152 per fortnight.

Gifts made in the five years before pension application are added back as assets, so there is a need for long term planning to achieve eligibility. There also exists a 'deeming rate of interest', currently 5% over this period, under the 'income test'.

The major concern with the gifting of assets is the 'older generation' losing control and having no financial security. I will discuss two options available.

An Acknowledged of Debt agreement, whereby the 'younger generation' are indebted to their parents for a limited sum, say $100,000. This amount is used because of the 'deeming rate of interest' mentioned above which would equate to approximately $190 per fortnight, and have a negligible effect on the rate of unicon, reducing it from $520 to $500. The 'older generation' retain some degree of control and financial security as well as receiving the pension.
Secondly an ideal situation would be to hold assets in a trust, as already discussed, the 'older generation' retain control of the assets, and are still eligible for the pension.
WHAT WOULD HAPPEN TO YOU AND YOUR FAMILY IF YOUR INCOME SUDDENLY STOPPED?

If an accident or unexpected illness stopped you working, eventually your income would stop, while the bills kept coming.

Now you can protect yourself against financial disaster caused by sickness or injury with the Income Protection Plan. This plan will ensure you a guaranteed continuing income when totally disabled.

This plan can provide benefits of up to 75% of your income from personal exertion less business expenses.

Who Can Apply?
You can, subject to the following occupation classifications, if you are under 60 years of age, and actively working.

Are My Premiums Tax Deductible?
The premiums in respect of your income protection benefit most certainly are. Whether you're an employee or self employed, your premiums are tax deductible under Section 51(1) of the Income Tax Act.

Do The Premiums Ever Increase?
Your premiums will automatically adjust if you accept Index Linked Benefit Increase; otherwise they will only change as you move from one age group to the next, remaining fixed for five years at a time.

THESE PLANS OFFER YOU

Guaranteed Benefit: If you suffer total disability, the benefit you applied for is what you are paid.

Waiver of Premium: Once the waiting period has passed, you will not be required to pay any more premiums if you are totally or partially disabled until you recover. Whilst we are paying you, you do not pay any premiums.

Guaranteed Renewal: We cannot cancel your policy or refuse to renew it because of your claims record, no matter how many claims you make.

SPECIAL OPTIONS TO MAKE YOUR PLAN EVEN BETTER

Crisis Benefit: A special help in time of crisis. If we receive confirmed diagnosis that you are suffering from most Cancers, Strokes, Heart Attack, Chronic Kidney Failure or Coronary Artery Disease requiring surgery, you will be paid a lump sum extra benefit.
Term Benefit - Pure Protection: Term benefit is the ideal form of Life Insurance if you're seeking greater protection for less cost.

Guaranteed Renewable, C.P.I. Indexation, Waiver of Premium: As you can see from this information, if you are seeking insurance this is the first cover I would advise you to take. Remember this is a plan to protect your income - your most valuable asset.

There are other forms of Insurance, in which you may find beneficial.

CRITICAL ILLNESS SECURITY PLAN

Low cost yearly renewable Term Insurance
The critical Illness Plan can provide lump sum benefit in the event of death or any of the following personal health crisis.

1. Heart Attack
2. Coronary Artery Disease Surgery
3. Heart Surgery
4. Stroke
5. Cancer
6. Quadriplegia
7. Multiple Sclerosis
8. Diplegia
9. Hemiplegia
10. Dementia
11. Parkinson's Disease
12. Major Head Trauma
13. Motor Neurone Disease
14. Renal Failure
15. Major Organ Transplant
16. Blindness
17. Major Burns
18. Liver Disease
19. Aphasic Anaemia
20. Occupational Acquired HIV Infection
21. Terminal Illness

Buy Back Option
This option allows the insured to purchase death cover without health evidence following payment of the Critical Illness Cover, with the exception of claims as a result of Liver Disease, Motor Neurone Disease, Occupational Acquired HIV Infection and Terminal Illness.

PERSONAL WHOLE OF LIFE PLAN is another form of cover you may invest in.

This plan combines the protection of Life Insurance and medium to long term savings for one fixed premium.

Attractive Tax Features: This means the company pays tax on investment income before sharing profits, the investment value of your plan is free from personal tax after ten years. This plan can also be used to build a solid foundation for your child's future. Funds are invested in the following areas.

Fixed Interest: Government and commercial securities.

Equities: "Shares" or "Stock" in Australia or overseas companies which are publicly investments.

Property: Generally high quality property in prime locations in Australia.
Others: These investments include cash, mortgage-backed securities options.

Term Insurance: This is a low cost yearly renewable insurance which provides financial assistance in the event of death or disablement.

This product can be used for:
- Mortgage Protection
- Partnership Insurance
- Income Replacement
- Spouse Insurance
- Key Employee Insurance
- Superannuation

WHAT IS SUPERANNUATION?
Personal Superannuation is a tax advantaged way to save for retirement.

Personal Superannuation Offers:
- A personal savings account for your retirement.
- A range of taxation advantages.
- The opportunity to roll-over any other Superannuation benefits into your account.

What Benefits are Provided by Personal Superannuation?
On retirement you may take the value of your retirement savings.
- As a lump sum payment, or
- In the form of a regular income from an annuity or pension, or
- A combination of both of the above.

On death, the value of your retirement savings will be paid to your dependants.

When can I collect my Retirement Savings?
You may collect your retirement savings when you have retired permanently on or after your preservation age.

Your Preservation Age
- 55 if you were born before 1 July 1960.
- 60 if you were born after 1 July 1964.
- If you were born between 1 July 1960 and 1 July 1964, the preservation age increases progressively from age 55 up to age 60 by one year for each year after 1 July 1960.

Annuities
Annuities are similar to fixed term deposits in that they pay an agreed amount of money regularly for a predetermined period. Annuities can have a fixed term or can be set up to pay investors over the rest of their life.

Allocated Pensions
Allocated pensions is a relatively new retirement income planning structure that only accepts superannuation or roll-over moneys. It provides the taxation advantage of annuities purchased with superannuation money. While offering the opportunity for the investor to determine and vary the income produced by the investment within a predetermined range calculated each year.
With allocated pensions however, the investor takes on the investment risk and there is no guarantee to how long the investment will last.

As we are brokers, we represent you to the insurance company so we have no allegiance to any one company.
PANEL DISCUSSION

If you were to die tomorrow......

Do you have a will?

Where is it?

Do you have a copy at home?

Who are the executors?

How are the assets left in your will?