



FARM BUSINESS SUCCESSION/TRANSITION

The 3 Circle Model In-Depth - From Confusion to Clarity

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AGENDA

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Topic: **The 3 Circle Model - From Confusion to Clarity**

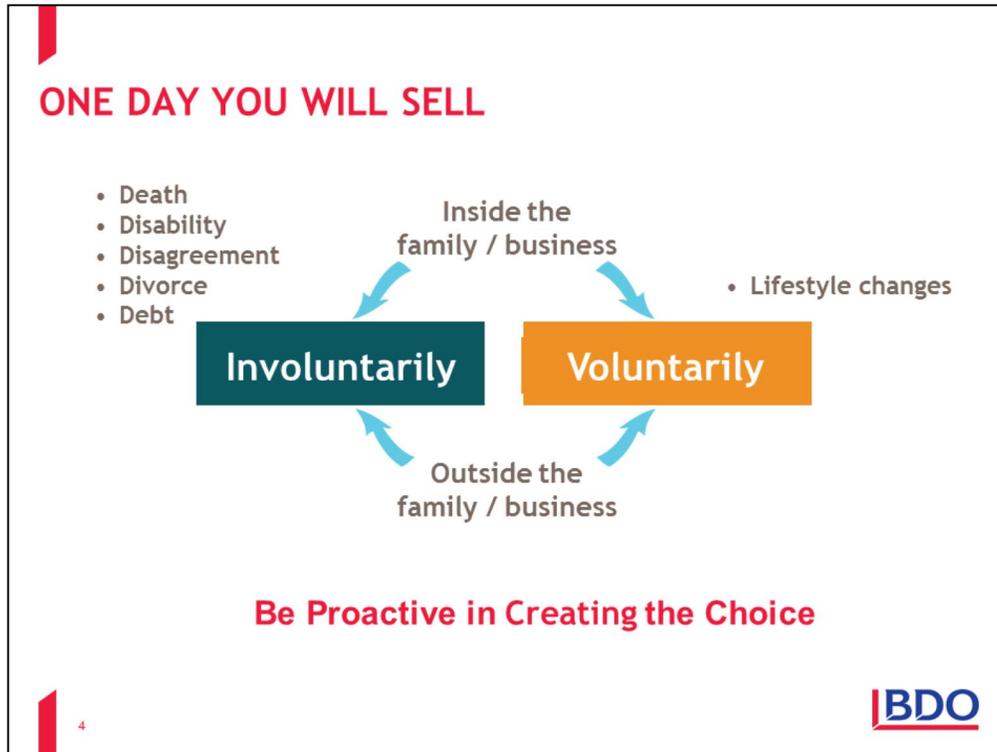
- Business Transition/Succession - Why farm families get “stuck”
- 3 Circle model
 - An overview of family, business and ownership circles
 - Differing perspectives
- Getting “unstuck”
 - Acknowledge and separate the issues
 - Use 3 Circle governance to solidify family relationships and professionalize farm business
- Technical Issues
- Q&A

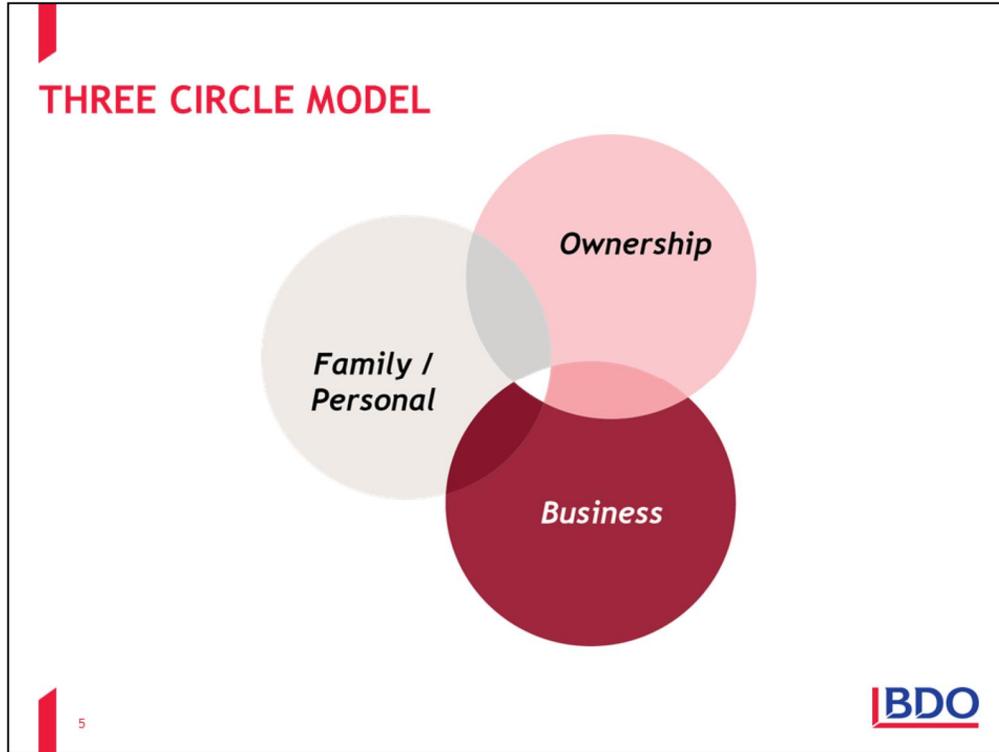
WHAT IS OWNERSHIP?

“Family Business” and “Family Enterprise”



Adapted from: Cunningham, 2015





WHAT IF YOU DON'T DO A GOOD JOB?



Why We Get “Stuck”

Advisor / client focus in succession planning

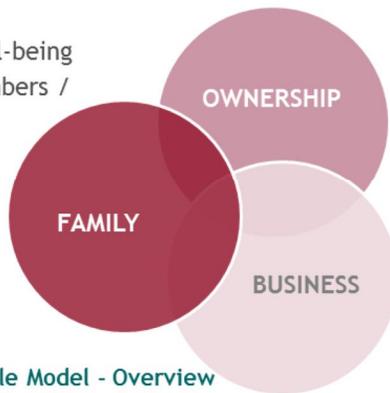
- Advisor - technical (e.g. tax and legal)
- Starting point?

Common results under traditional approach

- Documents, agreements, plans are not understood
- Unintended / undesirable outcomes
- Potential for conflict

OUTCOMES OF SUCCESSFUL IMPLEMENTATION

The personal well-being
of all family members /
partners



A cohesive ownership
group with a common
vision

A profitable and
successful business

3 Circle Model - Overview

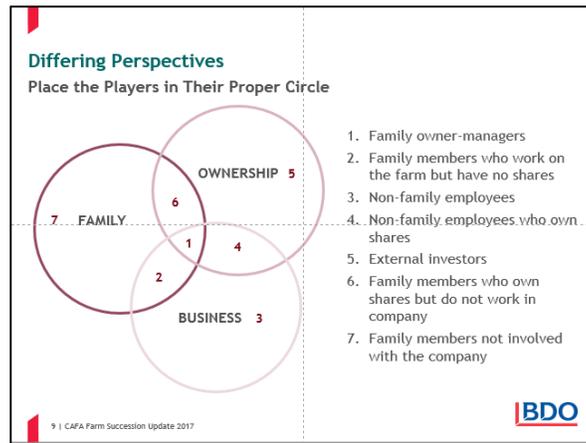
Image adapted from the 3-circle model by Tagiuri & Davis

Differing Perspectives

What you see and what you hear depends a great deal on where you are **standing**. It also depends on what sort of person you are.

- C.S. Lewis





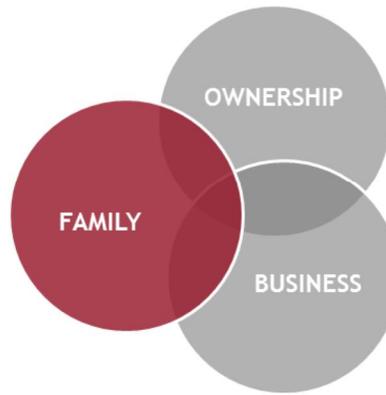
1. Family members who actively work on the farm and have some ownership (directly or indirectly)
 - “ Overwhelming challenge for controlling ownership group is have to deal with everyone’s concerns PLUS their own
 - “ Does anyone else care about the farm as much as I do?
 - “ What does life look like after giving up controlling ownership and decision making? Can I do that?
 - “ How much \$ do I need to retire and where will it come from??
2. Family members who actively work on the farm but do NOT have any ownership
 - “ What do I have to do to become an owner?
 - “ What do mom and dad’s wills say? Do they have an estate plan?
 - “ Will I have to be an owner with my non-operating siblings? Why does a 6 even get to be an owner when they don’t work on the farm?
 - “ Will I have to pay for shares or will they be given to me?
 - “ Will I be a farm hand for the rest of my life? Will I ever be trusted to make important decisions?
 - “ Why does a 4 think they can boss me around when they aren’t part of the family?
3. People who are employees but do NOT have ownership and are NOT members of the family that owns the farm
 - “ Worry about job security if owners don’t have a plan or if the plan doesn’t involve keeping the farm in the family!
 - “ Am I out of a job if Bobby decides to come home from college
 - “ Will I always be a hired hand?
4. People who actively work on the farm AND have ownership but are NOT from the family that has the controlling ownership of the farm
 - “ Worry about next gen family members who come back to the farm - WHY?? couldn’t get a job???
 - “ Worry about special treatment for family members (are they competent??)
 - “ Wonder about compensation for family members (is it fair wage)
 - “ Concerned about family issues (divorce, sibling rivalry) creeping in and impacting the farm
 - “ Do family owners (6s) really understand LT value of the strategic plan?
5. People who have some ownership in the farm but they are not family members and don’t actively work on the farm
 - “ RARE
 - “ Focus is on farm as a financial asset; performance; ROI
 - “ Will next gen run the farm profitably? What steps are being taken to ensure smooth transition?
 - “ No emotion; is it better for me to keep or sell this investment
6. Family members who have some ownership but DO NOT actively work on the farm
 - “ Should I be patient about getting \$\$ from the business?
 - “ Is the farm going to be profitable?
 - “ Often feel out of touch / uninformed about what’s going on
 - “ Prone to second guessing management
 - “ Is the farm just a financial asset to me or do I feel a sense of stewardship?
7. Family members who DO NOT work on the farm and DO NOT have ownership
 - “ Have opinions about future but lack power or influence
 - “ May be nostalgic about keeping farm in the family to respect elders
 - “ How can I teach my kids about what the farm means to me when I don’t own / work

Differing Perspectives

Objectives of the FAMILY CIRCLE

Emotional Centre

- Provide empathy and support
- Ensure fair treatment of all family members
- Includes ALL family members regardless of involvement in the business

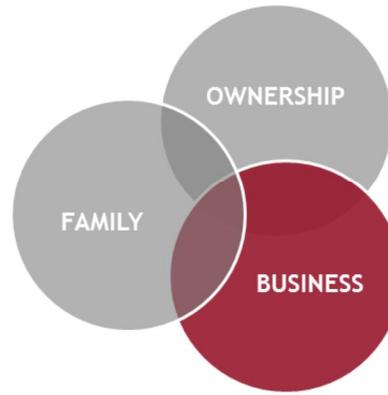


Differing Perspectives

Objectives of the BUSINESS CIRCLE

Wealth Engine

- Create opportunity
- Drive the business to be competitive
- Generate the wealth
- Satisfy the goals and vision of the owners

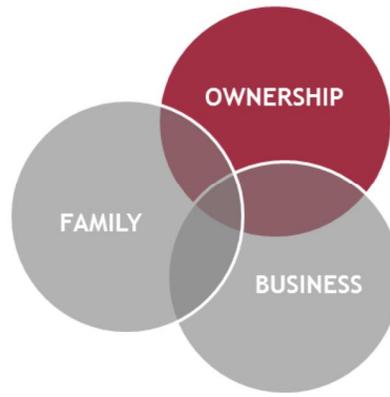


Differing Perspectives

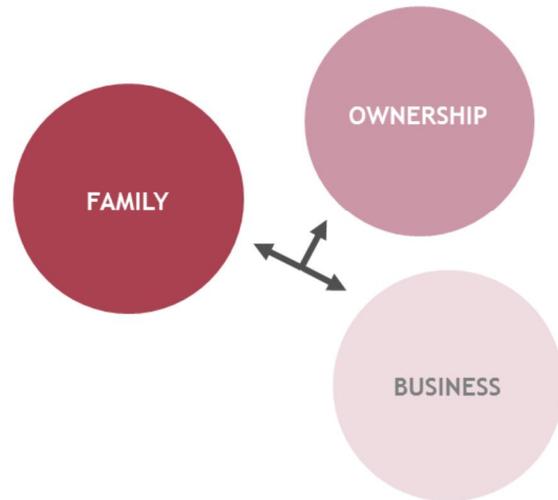
Objectives of the OWNERSHIP CIRCLE

Wealth Centre

- Ensure fairness and equity
- Build for the future
- Protect the wealth
- Stewards of the family business
- Plan for the unexpected



Getting Unstuck - Acknowledge and Separate the Issues



Getting Unstuck - 3 Circle Governance

- Family - traditions & celebrations
- Business - management and advisory
- Ownership - expectations & accountability

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Governance = communication and decision making

- “ Critical from the start
- “ Requires a bit of structure
- “ scalability

Family meetings

- “ Traditions and celebrations
- “ Family history
- “ Family values / mission / vision
- “ Education
- “ Code of conduct
- “ Resolving family conflicts
- “ Philanthropy

Business

- “ BoD - independent?
- “ Advisory board
- “ Strategic plan development and oversight
- “ Approve compensation and dividends policies
- “ Represent interests of ALL shareholders

Ownership

- “ Owners meetings
- “ Approve major transactions
- “ Review financial results
- “ Family employment policies
- “ How to evaluate and compensate family members
- “ Who can own shares in the business
- “ Dividend targets

Family trust

- “ Trust advisory committee

Overwhelming, yes, but as you move forward through transition / family grows will need some professionalization

Pick a circle you are primarily operating from; start to practice some of the concepts; recognize different perspectives, systems overlap (pebble in pond)



The best
ideas
emerge
when very
different
perspectives
meet.

- Frans Johansson

ESTATE FREEZE



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Tool to ease entry of family members into partial ownership, promotes

loyalty and dedication and possible succession to more full ownership.

ESTATE FREEZE

- Owners can “freeze” their ownership value
- Pass future value growth to the next generation
- Minimize and defer tax
- Maintain control through voting shares

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This tool helps enables the business owner to freeze the value of the business at a particular point in time by creating preferred stock, which does not appreciate in value, and then transferring the common stock to his or her heirs. Since the majority of the shares are preferred and do not appreciate, estate taxes are reduced.

An Estate Freeze is a tool that can be used to ease entry of family members into partial ownership. It

can promotes loyalty and dedication as there is a potential for succession to full ownership. By easing new leaders in to ownership you have the chance to evaluate them and assess their commitment to the vision of the future that has been agreed upon. You can establish goals and milestones for the new owners to meet before distributing more ownership.

FAMILY TRUST



FAMILY TRUST

- Trustees (usually parents) can hold shares and future growth “in-trust” for beneficiaries
- Helps defer decisions on who becomes an owner
- Can tie ownership distribution to attaining personal goals
- Protects shares from marriage breakdown
- Parents can take back shares if necessary

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The idea of a family trust is to protect the ownership of your assets. The trust provides a mechanism to pass family assets to future generations. This allows you to control how your wealth is shared. You can say when and how you want it distributed.

It is a way to give money in stages and allow children to best learn how to deal with it.

There are a number of pros to establishing a family trust....

“ Ensure your children not their partners keep their inheritance.

- To protect assets

divorce or marriage breakdown situation or in the event of death

- Control over assets held for the benefit of others
- Flexibility - in estate and succession planning
- Confidentiality
- Avoiding probate and succession duties

Providing for



Many business owners rely on their business to generate 100 per cent of their wealth, and are therefore invested in only one asset.

The largest share of the parents

financial investments for retirement is tied up in the farming operations. Nearly all of their personal assets are farm related.

WEALTH MANAGEMENT

Why should Owners build wealth away from the business?

- Protect wealth from risks of business
- Assist with retirement income and security
- Less need for cash flow from business
- Can be used to treat non-farming children fairly

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Think of building wealth outside your business not as a defensive strategy but as one that can give you financial security for the rest of your life and let you share your legacy with the next generation. Aside from diversifying your assets, creating wealth

the option of maintaining ownership of your business and

selling it when and if you wish.

At the very least, if we are able to set aside money for your retirement that is totally separate from the farm operation, you would have financial security for

LIFE INSURANCE



LIFE INSURANCE

- Create liquidity to pay income tax
- Can be used to treat non-farming children fairly
- Stabilize business in the event of death

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If everything is tied up in fixed assets when a major change happens, even the best managed farms can stumble.

The proceeds of a life insurance policy can be used to help cover the taxes payable resulting from the years of growth of your business. Δ

estate and possibly increase the amount of money you leave behind.

Talking about life insurance can be difficult and there are some upfront costs associated with finding the right insurance solution for you but these costs are nothing compared to the

COMMUNICATION IS KEY TO MANAGING RISK

Develop and communicate plans to protect wealth and ensure equitable balance that is fair to both the family and the farm operation.



Source: Preparing Heirs, Williams & Preisser



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People change, situations and circumstances change - be prepared

No one likes surprises when it comes to estate planning and family wills

*Secrets can cause family problems and destroy trust between family members
SO.....*

1. Start talking now

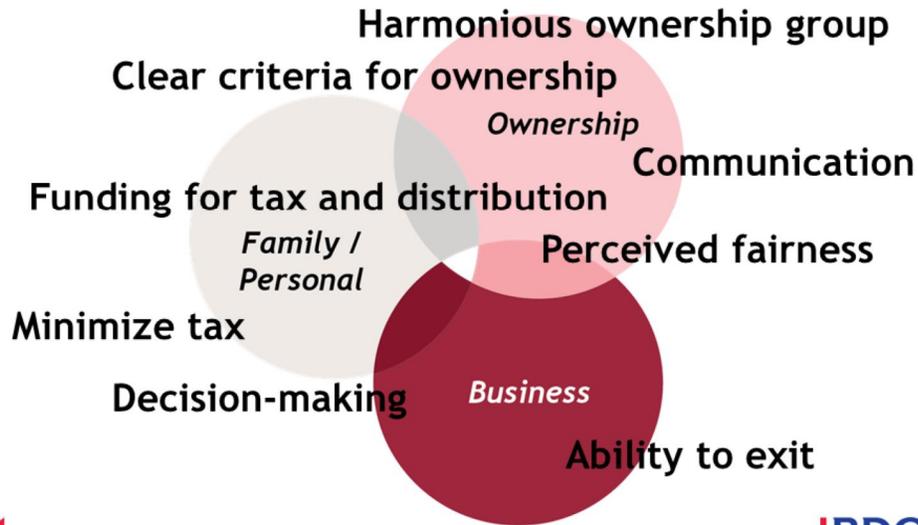
2. Put things in writing

3. Keep everyone informed

4. Expect the unexpected

5. Time very seldom solves problems - Deal with the issues now

WHAT IF YOU DO A GOOD JOB?



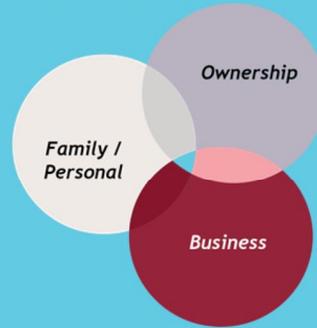
Imagine a future that includes:

- A harmonious ownership group
- Clear, agreed-upon criteria for ownership
- An ownership plan the family has contributed to and understands
- The perception of fairness amongst the family
- A plan to minimize tax
- Sufficient funding for tax and fair wealth distribution
- Good communication
- Good decision-making
- The ability to exit the business

BDO BUSINESS TRANSITION SERVICES

Helping You Build Your Bigger Future

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THANK YOU

