



PLAIN ENGLISH GUIDE

PENSION LAWS THAT AFFECT SUCCESSION PLANNING

Issues to consider if the farmer has more than a living area

- Security for older and younger generation - gradual hand over of business and lands
- Off farm investment including:
 - a) Insurance
 - b) Superannuation
 - c) Real estate
 - d) Diversification
- Motivation - The transfer to the younger generation can result in the following:
 - a) New technology and ideas
 - b) A good worker becoming a "bloody good worker"
- Don't just work for an asset you need to enjoy a good quality of life.

Case Study

The family owned 3,000 acres which easily supported three families. The parents owned 1,900 acres and were in their 50's and son A aged 26 who has a wife and three young children owned 400 acres and son B aged 30 owned 700 acres and had two kids.

Each son did not have had a viable farming area and if they sold the farm they could have purchased a house and maybe had a small surplus. The sale of the farm could affect the viability and maybe the family members might not have been able to acquire the property.

After consultation with the family accountant and insurance agent it was resolved that the business insure each son for \$500,000 on the basis that the son would leave their interest in the farming business and the farmlands back to the family members operating the business on the basis that the wife and the children would receive \$500,000 insurance. The family also put into place the following:

- a) Arrangements were made for the wills to be reviewed every two years.
- b) Mum and Dad had made arrangements to transfer the farmland over a period of time to the farming members on the basis that off-farm assets would be required for themselves.
- c) There was one family member off-farm and they resolved that a sum of \$40,000 would be paid to the non farmer who would have liked to be a farmer but due to being the youngest he had no option. The family assisted the non farmer when he needed help on the basis that the non farmer was to inherit non farm assets but as the parent were in their 50's the non farmer could have been waiting quite a long time.

Farmers with just a living area

Farmers with just a living area have to be cautious to ensure that they don't find themselves asset rich, income poor. Often a farm can support two families if both families can work on-farm and one family can obtain off-farm income.

A major problem arises as to what happens if one family wants to retire or one family member can no longer work? The issues to consider include the following:



- The social security five year rule states that a gift today of the farm to a child is not classed as an asset under the assets test in five years time.
- The assets of a farmer can be reduced if farmlands are transferred to the person or persons operating the farm taking into account foregone wage.
- The assets can also be reduced if the farmlands are transferred subject to the parents right to live on the farm (granny provision rights).

People who have just a living area should give consideration to transferring their farmlands at least five years before they reach retirement age. The security of the older and younger generation must be considered.

Below are some examples as to how a person with just a living area can plan for the future.

Case 1: Transferring by way of gift at least five years before retirement age

Parents own a farm which is debt free. Their daughter and son-in-law work the farm and they have one child, a teenager, who would like to be a farmer, The aim of the parents is to stay in the business but to dispose of their major asset, the farm, prior to retirement.

The aim of the exercise

- a) A second mortgage can give the parents a nest egg which they can use to purchase a car or carry out improvements at a later date. Importantly the daughter and son-in-law can operate and not borrow further funds without the approval of the second mortgagee (the parents)
- b) Parents stay in the partnership. The capital accounts need to be monitored.
- c) Five years after the transfer, Mum and Dad will qualify for the pension under the Assets Test.
- d) In the good years the farming business could distribute income to Mum and Dad and their pension would be reduced and possibly cancelled. In the bad years Mum and Dad could get a pension.

Case 2: Transfer of farm taking into account foregone wages

Commins Hendriks was involved in a matter where the parents and two sons were farming the farm. The parents owned farmlands valued at \$400,000 and the sons owned small blocks. The parents were disqualified from obtaining a pension under the Assets Test and it looked like the farmlands would have to be sold which would have resulted in the sons and their families having to leave agriculture.

However, the transfer took place on the basis of the following:

1. Value of farm \$400,000
2. Less value of foregone wages \$200,000
3. Balance parents' assets \$200,000

The sons had worked for sheepdog wages (a good feed, a kick in the behind occasionally) and obtained pocket money by working off-farm aged 16-21. Foregone wages are calculated as follows:

1. There must be a legal transfer of the farmlands.
2. The value of the wages at current day rates.
3. Foregone wages can include the value of any improvement carried out and the value of income not received. The Foregone Wage Provisions do not apply for the period the family member is involved in a partnership or share farming arrangements. (Copies of the guidelines for calculating foregone wages can be obtained from any Centrelink Office).

The above was a great success story as it enabled mum and dad to retire and get virtually the full pension and insured that the two sons farming could remain viable.



Case 3: Transfer of arm taking into account the Granny Flat Provisions.

Farming couple are aged 70 and the value of their assets prevented them from getting a pension. If the farm is valued at \$400,000 then they would be prevented from getting a pension. However under the Granny Flat Provisions they could transfer the farm to persons operating the farm and if they had the right to stay in the house on the farmlands being transferred then the value of this would be \$172,996.82 under the Granny Flat Provisions. The value of the Granny Flat Provision varies depending on age and the life expectancy of the youngest member of a couple multiplied by the maximum combined rate of pension.

The transfer would have resulted in the following:

1. Value of farm \$400,000
2. Less value of Granny Flat Provision Rights \$172,996
3. Net value of farm \$227,004

The parents could qualify for a part pension.

A copy of the guidelines in relation to the Granny Flat Provisions can be obtained from any Centrelink office.