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Family farm succession and its taxation implications

Georgiena Ryan | Principal Lawyer

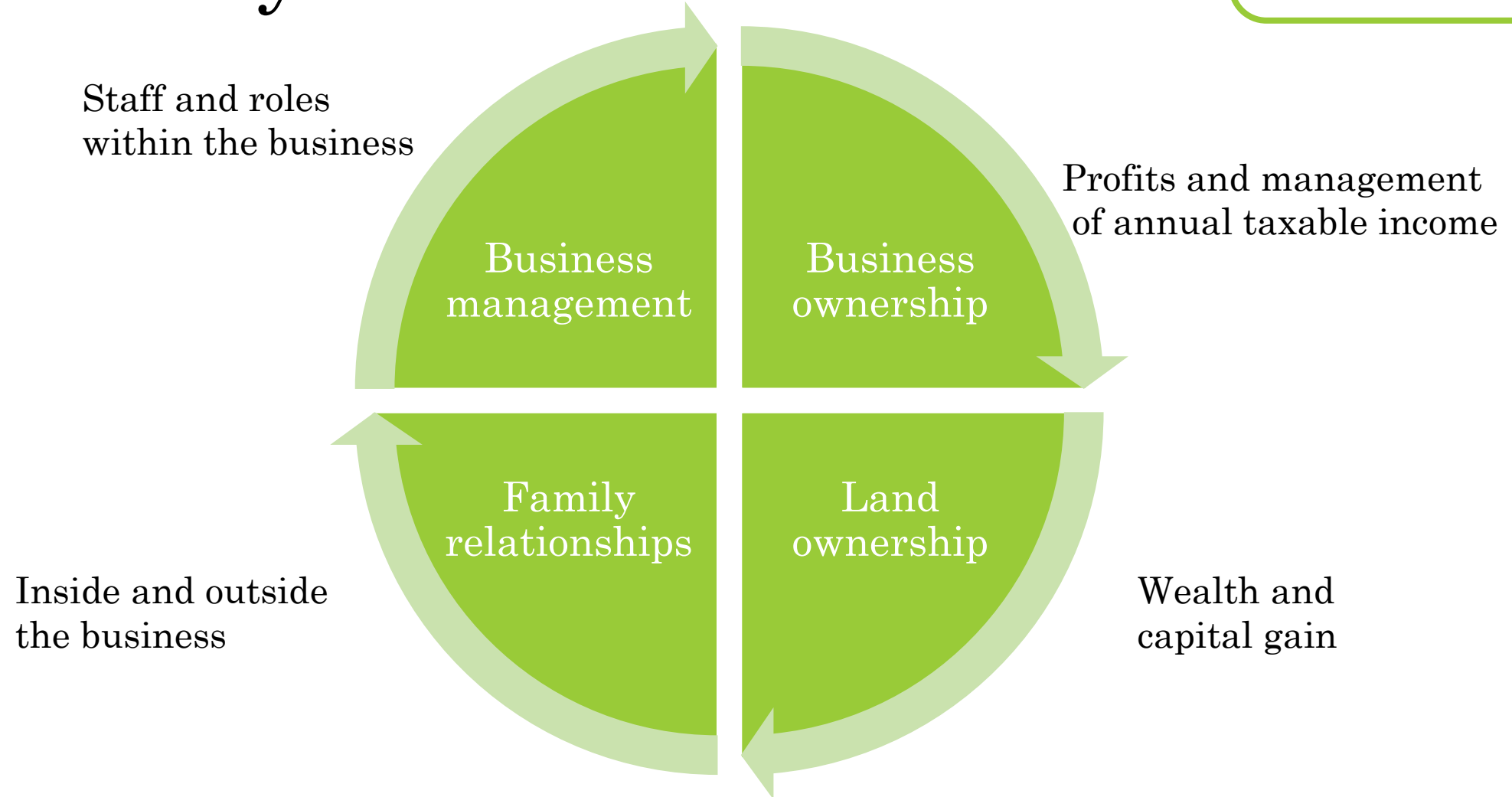
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Family Business Succession



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Lets talk about CGT and the great wealth transfer



If I am 55, in 1985 my parents were probably 40

If I am 50, in 1985 my parents were probably 35

If I am 40, in 1985 my parents were probably 25

If I am 35, in 1985 my parents were probably 20 and
my grandparents were probably 45

If I am 30, in 1985 my grandparents
were probably 40

If I am 20, in 1985 my
grandparents were probably 30

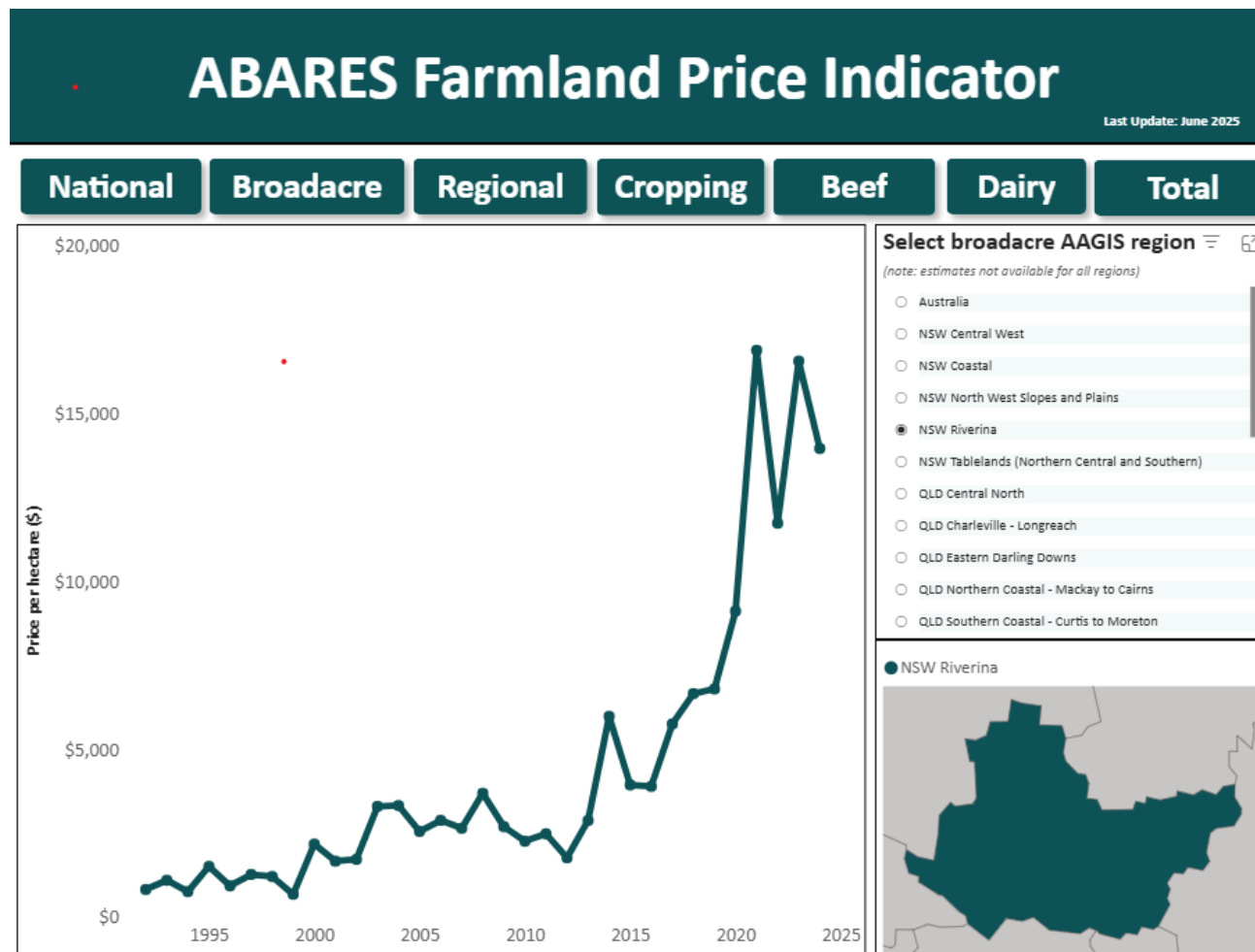


The basics of CGT



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1. Ted bought 1,000 acres of land in 2002 for \$800/acre. At the time of buying the property the costs involved were about \$40,000.

2. Ted's "cost base" is \$840,000.

3. Ted is offered \$4,000 per acre by a neighbour to sell = \$4,000,000.

4. The capital gain is $\$4,000,000 - \$840,000 = \$3,160,000$.

5. In the year he sells, Ted's farming partnership that comprises Ted and his wife makes a profit of \$120,000.

6. Ted's income for that year is then \$60,000.

7. Under the current CGT rules, the capital gain is divided by two: \$1,580,000.

8. This is added to Ted's income of \$60,000.

9. Ted pays tax that year on income being \$1,640,000.

10. The tax payable will be \$704,138.

*From 1 July 2027,
this is changing.
The cost base will
be indexed against
CI*



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**At market value
and when you
gift it, I will
take my share**



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Resetting or putting off CGT



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Small Business CGT Concessions

- \$6,000,000 net asset test
- \$2,000,000 turnover

Rollovers

- Death
- Divorce
- Small business restructure (*different test*)

Small business CGT Concessions

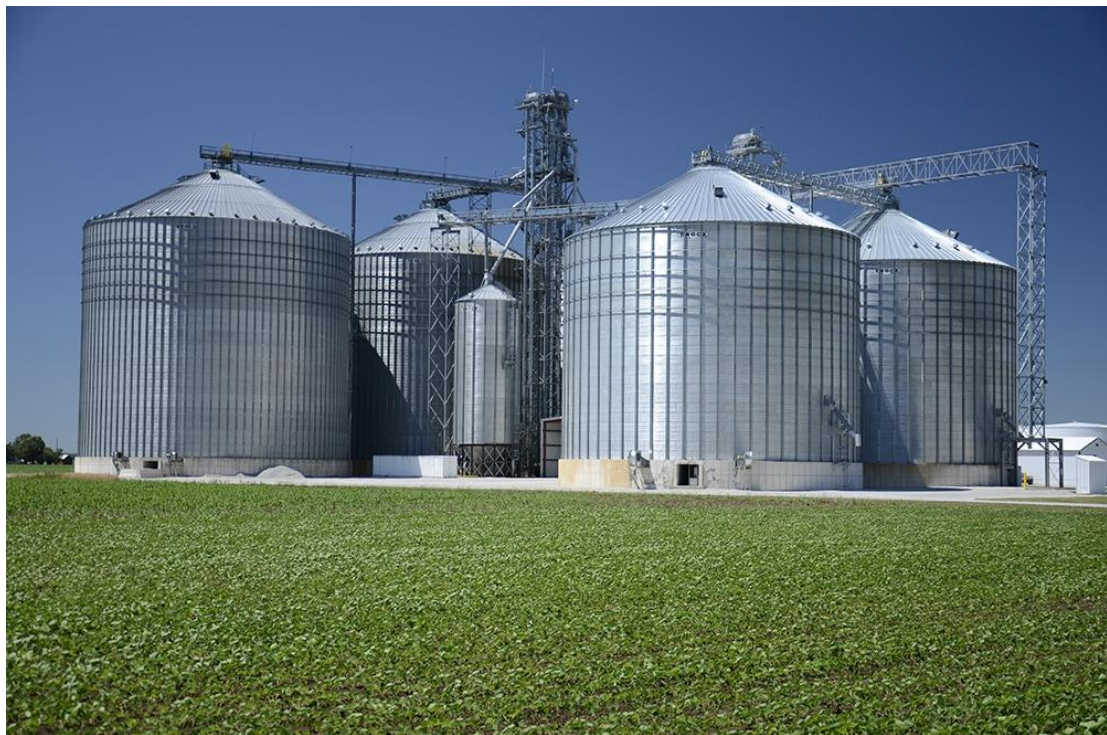
- 50% active asset reduction
- Small business retirement exemption
 - Don't actually have to retire
 - \$500,000 lifetime limit
 - Requirement for proceeds to be paid into super if under 55
- Roll-over
- 15 year exemption
 - Has to happen in connection with retirement



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CGT Affiliates



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Small business restructure roll over relief

- Available to businesses with a turnover of greater than \$2 million but less than \$10 million
- A new entity is created as a part of a business restructure (e.g. go from operating as a partnership to a company)
- The new entity “inherits” the asset at the *cost base* from the other entity (the original purchase price / value)



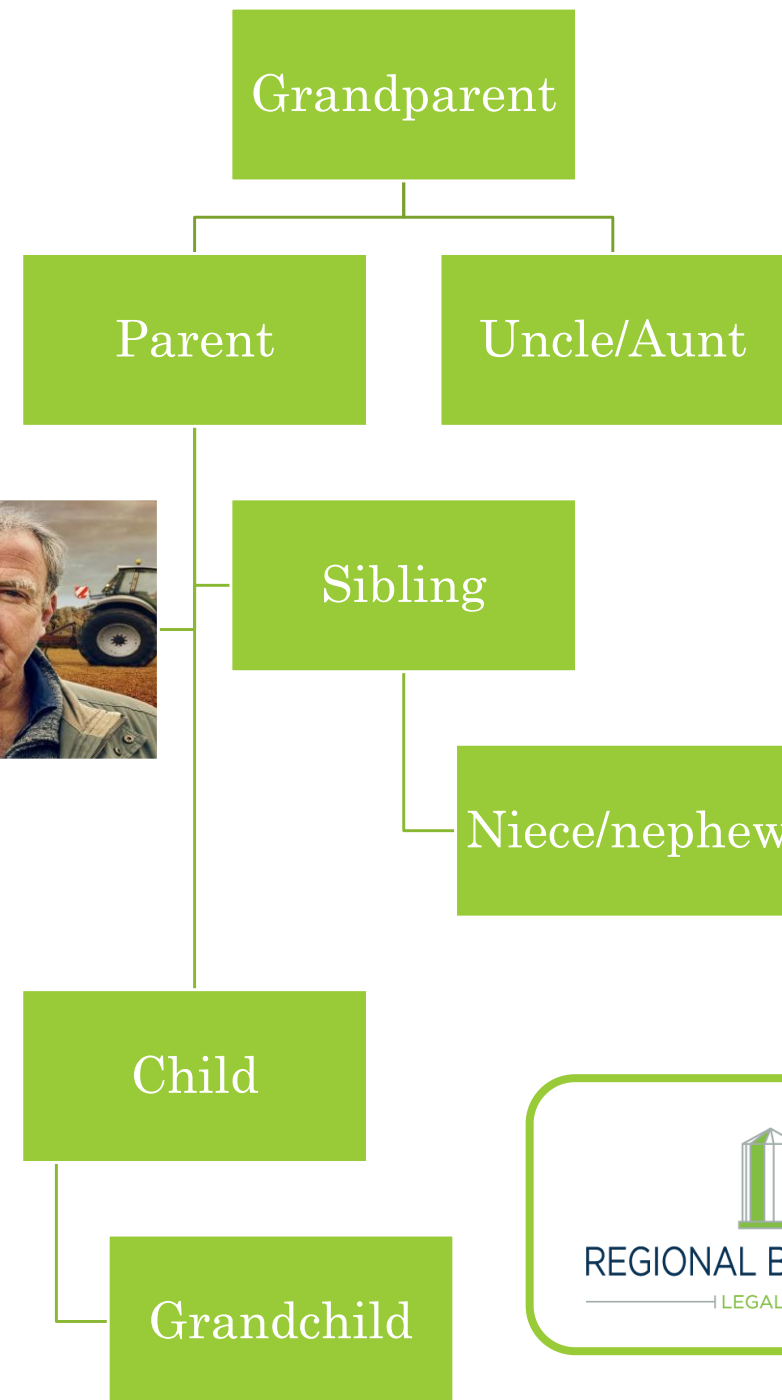
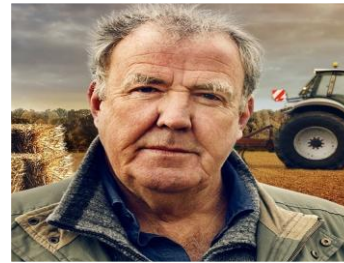
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Stamp duty concessions

- Exemption from duty for the transfer of assets between family members.
- This exemption extends to transfer of assets between entities controlled by related family members.
- The asset must be used in a farming business by a family member (or entity)

Spouse



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Other entities

- Companies:
 - Entitled to vote
 - Entitled to 25% on a winding up
- Discretionary trusts
 - Entitled as takers in default to 25% of the capital on a winding up
- Superannuation fund
 - A member
- Deceased estates
 - The deceased

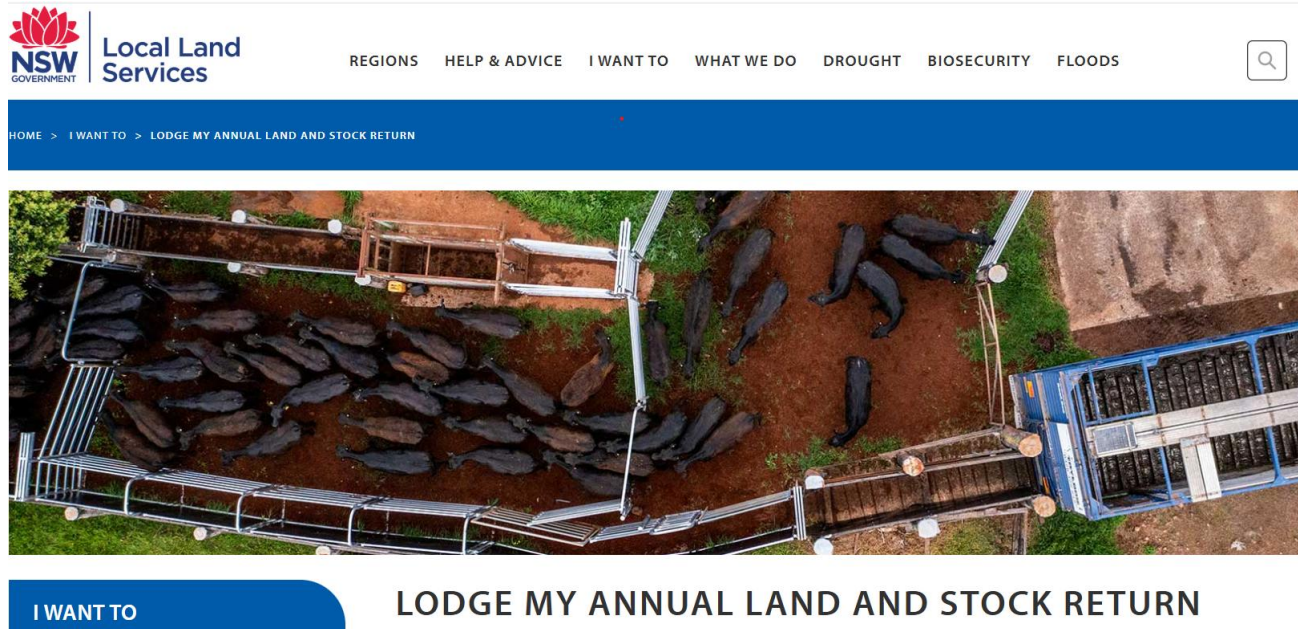


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Proof of a primary production business

- There must be a primary production business being carried on by:
 - A member of the family before (includes other entities)
 - And after by the transferee or an entity controlled by the transferee



Transfers under wills & CGT

- A gift under a will is not subject to capital gains tax.
- The beneficiary receives the asset at the “cost base” of the person who has died.
- If the deceased owned the asset before the introduction of capital gains tax, then the beneficiary receives it at market value on the date of death.
- **This will change under the new rules**, in that the beneficiary will receive an asset bought before 20 September 1985, at the value as at 1 July 2027.
- **There is typically no stamp duty on assets gifted under a will.**



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Estate disputes

- FAMILY PROVISION
- DURESS/UNDUE INFLUENCE
- CAPACITY CLAIMS
- PROMISSORY ESTOPPEL
- SHAREHOLDER OPPRESSION
- TRUST CLAIMS
- PARTNERSHIP CLAIMS
- SUPERANNUATION DISPUTES



The cost of litigation



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Take instructions and engage a barrister to give you advice	\$30,000
Issue a statement of claim	\$5,000
Further and better particulars	\$10,000
Directions hearing – flying to Sydney	\$13,500
Defence and cross-claim	\$15,000
Further defence and second cross-claim	\$10,000
Further directions hearing	\$13,500
Obtain evidence	\$75,000
Mediation	\$10,000
More evidence	\$35,000
2 week court hearing	\$240,000
TOTAL	2 to 5 years of your life + \$457,000

Transferring business assets & CGT

- There are complex consequences for transferring business assets.
- There are some rollovers available, however it is important to get specialised advice from your lawyer and accountant.



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Understanding your current position

This is crucial in succession planning to understand what options and concessions may be available to you.

To understand your current position, ask the following:

- Do we know who owns what land in our business?
- If the land is owned by a company, do we know who the directors and shareholders of that company are?
- If the land is owned by a trust, do we know who the trustees, the default beneficiaries and the appointors of that trust are?
- Do we know **when** that person or entity purchased that land or had it transferred or gifted to them?
- What the purchase price was or what the market value was on that date?
- What is the potential capital gain if we were to sell or transfer that asset now?
- What is our business turnover?
- Have we taken into consideration the potential capital gains tax payable when working out what equity and fairness looks like in our succession planning?

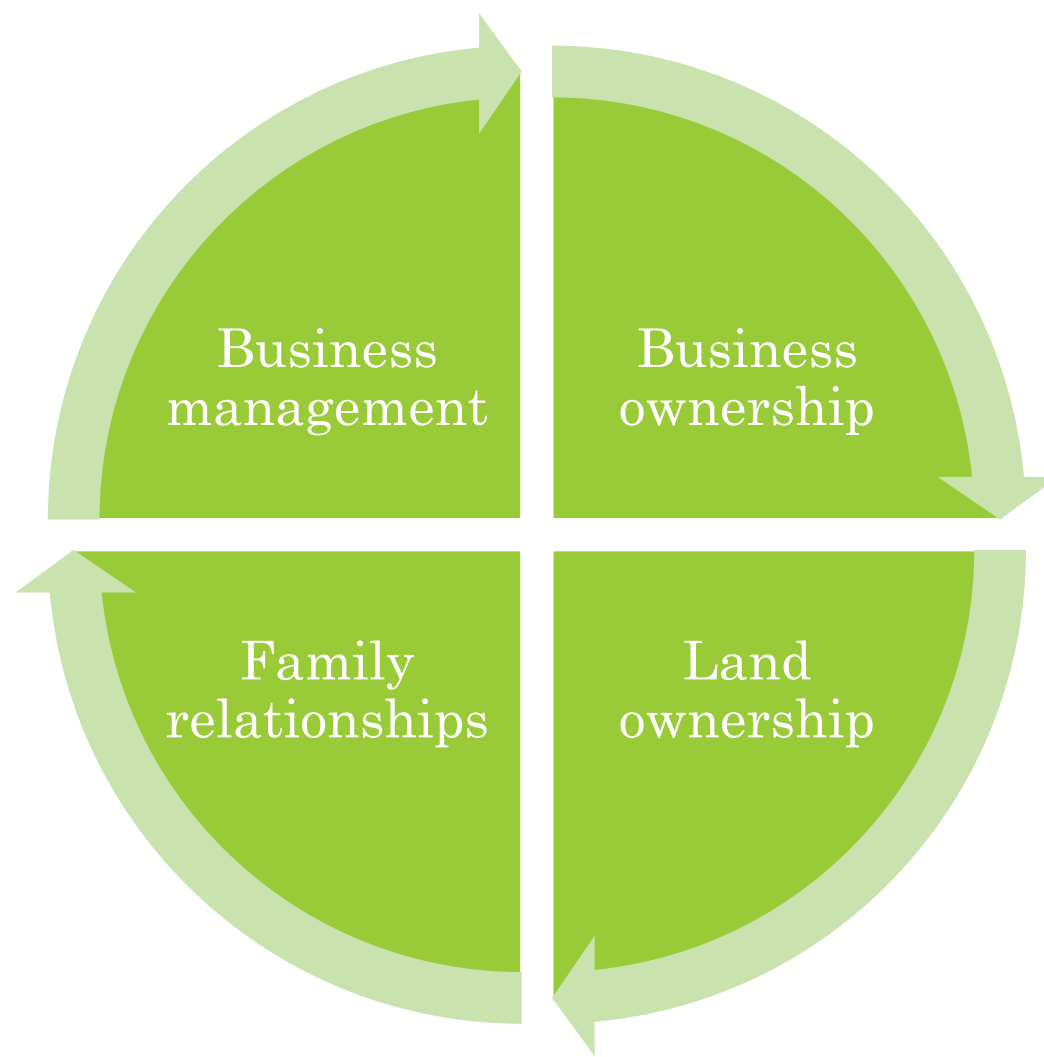


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To understand your current position, ask the following:

- How are we going to account for the contingent CGT liability in our future planning?
- Is there an opportunity to take advantage of CGT concessions this year that might not be there next year?
- What investments have we made into our staff and management expertise that will improve the business?
- What investments have we made into our family relationships to avoid “*Succession – The Complete Series*”?
- If our land is held in a company or trust, do we need to make any amendments that might allow us to take advantage of a stamp duty concession at a future time?
- Is there anything in our financials that might cast doubt on the beneficial ownership of an asset and if so, can we address it?
- When making the decision on the purchase of a new header/spreader/seeder or even a new property or other capital asset have we considered the alternative of making an investment to fund long term succession needs?



Family business succession

Entities

Partnerships

- Simple
- Easy access to FMDs
- Income split in a set manner
- Can have salaries
- Carry forward losses
- Partners personally responsible for debts of partnership
- Be aware of presumption of partnership

Companies

- Shareholders
- Directors
- Income split between shareholders
- Income can be retained in companies
- Flat tax rate
- No access to 50% general discount
- Limited liability of shareholders
- Directors generally limited but:
 - Statutory liability
 - Trading while insolvent
 - Breach of directors duties



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Entities

Trusts

- Complex
- Access to FMDs
- Income split in a flexible manner
- Can have salaries
- Cannot distribute losses
- Trustees liable for debts
- Be aware of beneficiary loan accounts
- Its all about control

Self managed superannuation

- Trustee
- Members
- Income retained until meet retirement age, death or other legally allowed reason for distribution
- 15% tax and no tax when in pension phase (generally)
- 30% general discount
- Holds assets only
- Need for binding death benefit nominations

Family business succession

- Family agreement
 - Overarching agreement covering the whole family
 - Spells out intentions regarding holistic view of business, transfer of business, transfer of farmland and estate planning
 - Build in non-monetary measures
 - Succession Act Release
 - Separate Binding Financial Agreement





Family business succession

- Ownership agreements
 - Leases
 - Options to buy
 - Mortgages and loans
 - “the Byron Bay clause”

Family business succession

- Business management agreement:
 - What are the values of our family business?
 - What are our roles in our family business?
 - What is our expectation about our commitment of time to the business?
 - How does our family remunerate the people involved in our business?
 - How do we make decisions in the business:
 - Every day decisions
 - Important decisions
- What happens:
 - Death
 - Divorce
 - Disaster
 - Default



Who do you involve?

- Your accountant
- Your solicitor
- Your bank
- Farm consultant
- Financial planner
- Succession planning facilitator



AFTER A FEW SECONDS, THE 'ROUND TABLE'
NEGOTIATIONS HAD ALREADY FAILED.



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This presentation contains a summary of tax and duties issues only. It is for educational purposes and does not constitute legal advice.

Our team





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Regional Business Lawyers
Suite 2A, 77 Gurwood Street, Wagga Wagga NSW 2650
(02) 6925 8256
reception@regionalbusinesslaw.com.au

www.regionalbusinesslaw.com.au



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