# *Planning for Unexpected Future Events*
# *The 5 D’s*

## Risk Management

Evaluating risks associated with the continuation of the farm business is the first step in developing a plan to address and/or reduce these risks. The worksheet “5 D’s Management Plan” is a way to assess and evaluate the risks that your proposed business arrangement will face.

The following discussion about planning for these risks will provide information for you to consider in evaluating your risks and developing a plan to reduce these risks. Developing a risk management plan should begin with developing family, business, and personal goals. If you have identified these goals in the “People Considerations” section then you can begin the process of developing a plan to reduce the risks associated with accomplishing these goals.

## Planning the 5 D’s

Sometimes in the enthusiasm, hope and excitement that accompany the establishment, expansion or transfer of a business to the next generation, we forget that even the best laid plans sometimes do not work out. Therefore, even though we may be reluctant to discuss negative issues, it is critical to discuss the cons as well as the pros of any business venture. While we cannot control the future or plan for every eventuality, exiting or entering farming is a major life decision that requires us to make provision for events which could impede or even destroy the farm transfer or the farm business.

There are five major events that can severely impact a farm family or a family business: **death, disability, disaster, divorce and disagreements--the five D's**. Planning a farm transfer without providing protection against the possibility of any one of these major events is gambling with your future and your family's future, whether you are entering or exiting or modifying the farming business. Most people don't like to talk about these issues, or develop and put in writing contingency plans for addressing them.

How a family deals with these issues will likely affect the farm transfer process. For example, the operation may be able to continue if the spouse that does not provide labor to the farm business dies, but what if the person providing the major labor and/or management dies or is disabled or incapacitated for a long period of time? How long of a period of disability can the operation survive? Should there be life insurance? Should there be disability or income continuation insurance to cover the major contributors? How can we protect the transfer assets from being sold off or divided in the event of a divorce? How much crop insurance, liability insurance, casualty coverage should there be? How will a major illness or injury affect the operation? Do we have enough health insurance to avoid an impact on the business finances in the event of a major illness or injury? What happens if a major disagreement results in one or more of the farm operators leaving the farm business and withdrawing farm assets.

## Death

Life insurance can provide protection for families and/or the business in the event of a death of one of its members. For young families who generally have higher debt and less cash to work with, term life insurance may offer an attractive and low cost alternative to whole life or other investment protection. Term policies do not have a value except upon the death of the insured.

Younger farm members may want to carry life insurance on older members who own most of the farm assets in order to be able to continue farming in the event of an untimely death. The premium cost may be very expensive but this may need to be one of the costs to insure the continuation of the farm business. Other options need to be discussed and planned for, so the younger generation is able to gain control of assets in the case of a premature death of older members who own most of the farm assets.

## Disability

Providing for income protection will also be important in the farm business. Disability or income continuation insurance can provide the dollars to cover extra family living or hired labor expenses during the period of disability. Farming is not only a risky business, it is a dangerous occupation. Farm accidents and farm related illnesses affect thousands of farm families annually.

Farming is categorized as the single most dangerous occupation in the United States. Given these facts, it is important to take appropriate action to minimize risks to the family and the farm business.

Insurance coverage can be purchased to cover people in the event of a disability. But another kind of precaution should be part of your farming operation. Prevention should be a key plan of any farm business. Prevention of farm accidents and farm-related illnesses begins with a thorough review of the farming operations, farm tasks, farm machinery and equipment, farm buildings, electrical service, watering systems, well, septic system, and farm topography. Even routine tasks should be analyzed to ensure that safety is built into every aspect of the operation. We have all seen situations that are "accidents waiting to happen." Being alert to your surroundings will help you and your family continually identify potential hazards and take action to mitigate harmful situations. This “insurance” is one of the best protections you can have for your farming operation.

## Disaster

When we hear the word "disaster," we generally think of natural disasters like a tornado, drought, or flood. A broader definition could include any major event or circumstance which has a severe impact on the farming operation. These might include stray voltage, contaminated feed or water supply, a manure or pesticide spill. All of which can put the operation in financial jeopardy.

The United States Department of Agriculture (USDA) has been the agency to provide disaster assistance to farmers who experience crop losses due to disaster. Disaster benefits have been generally available to eligible farmers whether or not they were program participants and whether or not they were covered by crop insurance.

Because of significant costs to the federal government due to disasters of recent years, including hurricane Andrew in 1992 and the Midwest flood of 1993, the USDA is phasing out of disaster programs. Being aware of changes in the disaster and insurance programs and planning for how your operation will adjust to them are important considerations in your protection against disaster.

Analysis, mitigation, and prevention are the best insurance against other disasters such as stray voltage and water contamination. A farm's electrical, water and waste disposal systems as well as all mechanicals should be checked by certified professionals prior to purchase. Thereafter, systems should be checked on a regular basis. Farmers also need to watch for any changes in the behavior of their livestock so that corrective action can be taken immediately.

Because a disaster can have such a sudden and severe impact on a farming business, it is important to consider both the insurance and prevention avenues available for your farming operation. Additionally, when at all possible, you should set aside savings or other non-farm investments which can be available to you in the event of a disaster.

## Divorce

We know that death in inevitable. But divorce is something most people prefer not to talk about, or plan for. Yet, we know that as many as one out of two marriages ends in divorce. Coupled with other risks involved in farming, the potential for a divorce cannot be ignored. Facing the possibility up front can alleviate some of the uncertainty in the farming business in the event of a divorce.

It is important to have a marital property agreement which lists all assets and debts as well as all ownership and management responsibilities. You should be aware, however, that even with a marital property agreement, divorce property division rules may mean that the court will find the agreement inequitable or unenforceable. Therefore, the provisions of any marital property agreement should be thoroughly discussed between the parties and be reviewed by each with their own separate attorney prior to signing.

## Disagreements (Conflict Resolution)

Major disagreements may emerge over time with multiple farm families involved in a farm business arrangement. Persons and their circumstances change overtime. As younger farm personnel get married and have children, their circumstances, values and goals may become quite different than when they entered into a joint farming operation with their parents or other unrelated persons.

The hours involved in most farm operations are long which leaves little time for family. This can easily cause friction in the farm business. The management view point of one member may become more divergent from other managers in the business.

Disagreements over capital allocations can cause friction between farm families. The speed at which farm assets are transferred to the younger generation can cause tension between the differing generations. The level of debt in the farm can cause difficulties. The older generation generally wants to reduce debts as they near retirement. Any number of personal difficulties may develop between persons or families involved in the joint farm business. At times this may mean some families will leave the farm business and pursue other employment opportunities. This may be disruptive to the farm business arrangement, especially when the departed member has substantial ownership of farm business assets.

All parties should know in advance what the financial implications will be when a future separation occurs. This is every bit as important as the arrangement for entering the farm business arrangement.

A plan needs to be developed at the time of commencing the business arrangement as to how multiple farm business families will sever their joint farming operation. Generally a plan is needed where departed members receive only part of their investment at the time of severing the joint farming operations. Some number of years for the payments should be established when the agreement was originally formed.

When developing a business arrangement it is important to consider how to take it apart if it is not working. If it is organized in a way that makes it difficult to take apart it may be best to consider alternative arrangements.

## *Exercise*

# *Developing a Risk Management Plan*

Use this worksheet to assess and rank the 5 D's for your business arrangement. Start by keeping in mind the business, family, and personal goals of the people involved. List the present plan in column titled "Current Risk Management Plan". Next list the risks not addressed in the next column. Rank the possibility of this risk occurring in the next column. Then consider the impact on meeting the identified goals if this event were to occur. After completing these columns the 5 D's rank the risks in priority from 1 to 5 or as high, medium, or low. The last step is to identify steps to take to manage these risks. These steps become your risk management plan.

The plan should be reviewed and updated as changes occur in the business, the people involved, and as goals change.

# *5 D’s Management Plan*

| Risk | Current Risk Management Plan | Risks that are Not Addressed | Possibility of Risk Occurring H-M-L | Impact if Risk Occurs H-M-L | Priority of Risk | Steps to Take to Manage Risk |
|---|---|---|---|---|---|---|
| **Death** | | | | | | |
| **Disability** | | | | | | |
| **Disaster** | | | | | | |
| **Divorce** | | | | | | |
| **Disagreement** | | | | | | |