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The Farmer's Pension Plan – A New Type of Financial Genetics

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The Farmers Dilemma:

So how are you going to do it? I mean, how are you going to ensure that the kids who want to farm can – without leaving the non-farming kids out in the cold? What about your retirement income?

It is difficult for farmers to enable their children who want to farm, provide for their retirement income, and to have something for the non-farming children. We want all our children to be happy in their chosen employment fields and to be enthusiastic cheerleaders for each other at family gatherings. Family harmony is central to the farming family tradition.

Usually, the financial industry has recommended insurance as a way to compensate the non-farming children. I would like to suggest that another "bull" with different genetics be added to the financial semen tank. I call this bull the "Farmers Pension Plan." It is a different, more flexible and profitable method for managing farms through the human life cycle. It also eliminates the insurance premiums that don't build equity – similar to renting a home instead of owning. It works for most businesses as well, but especially farming, since the farm can be transferred on a tax deferred basis to the succeeding generation.

First, let's look at the typical insurance model using some kind of whole life policy. The benefits are clear – in a joint last to die policy for a husband and wife, there will be a payout that can be used to pay the non-farming kids a significant inheritance (millions if you so choose) without straining

the farm(s) at the second parent's death.
I recently priced an insurance policy for a farm husband and wife in their forties and assuming their health is good, they would be paying about $7,000 for each million of benefit on the second death. To make a dent in their expected farm value in 40 years, they would need at least 4 million costing $28,000 per year for life. Umm, that is kind of a lot of money disappearing from a farm's milk cheque that still wants more land and quota. Will the farm still be able to pay that amount 30 years from now when the farm might not be as profitable as it is now? On the good side, inflation will erode the premium, but also the benefit perhaps by 50% or more over those 30 years. How do we know how much money we will need for the non-farmers? We don't.
As our kids grow up and start families of their own, they enter a period of significant financial distress – down payments, mortgages, hockey skates, ballet lessons etc. And then we just hope they don't get divorced. If ~$28,000 per year is leaving the farm, where is the money going to come from to help young adults and your grandchildren when they most need it? I expect you will work harder and longer as this is what farmers do when necessary. Your 60 year old children may want and appreciate a cash infusion when you pass away, but they are not so likely to need it as they would in their 30s.

So here is another idea, one that addresses the expansion of the farm in the present, provides for an income to the retiring farmers, allows for support of young families, offers flexibility in costs and can be wound down at any time.

The Farmer's Pension Plan – The New Bull in the Tank

<u>The Mechanics:</u>
First, we borrow 1 million (example) from the banker to fund the investment program. The interest rates are very low right now and I believe will be for some time (my opinion). Low interest rates are key to the strategy. My clients will use my investment services. This cost should be tax deductible. At that 10 year point, we hope to have the loan paid off by the farm or income from the investments. We also expect that the fund will have grown to be 2 million dollars in tax efficient investments from which an income of $80,000 per year or 4% can be conservatively withdrawn. This allows the farmers to retire, hopefully live on the farm, but not need to draw an income from the milk cheque. On some farms, it may be beneficial to take out 10 year term insurance policies in case husband or wife dies in the 10 year period. These are inexpensive for younger, healthy people. I don't work for RBC Insurance, or any other individual company, so I use whichever quality insurance company is offering the lowest cost.

<u>Flexibility:</u>
This Farmer Pension Program can be wound up or modified at any point. For example, the farm next door comes up for sale. This can be a once in a lifetime deal requiring financing. The whole life policy program is now a liability with its cash drain, but we can change the pension plan to make the purchase more attractive to the bank.

<u>Retirement Plan:</u>
At the end of 10 years, if we haven't needed to raid it, there should be roughly 2 million in the Farmers Pension Plan to support retiring farmers. Meanwhile the insurance policy continues to remove the $28,000 premium each and every year. At the end of life, the Farmers Pension Plan is there to support the non-farming kids. This is when the insurance also pays out and the premium payments stop. This, a straw of semen to keep in your back pocket, it isn't for everybody, but having some different genetics available is a good thing.

I wish you all a great end to the cropping year!