

# FARM BUSINESS FACT SHEET



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## KEY POINTS

- Farm generational transition can start well before the older generation is ready to retire. Commence with the transfer of management responsibility. Asset transfer should be the final focus
- Financial security in retirement for the parents is the first and most important objective
- Generations farming together and sharing business profits and access to land can be an important interim step
- If both generations are farming together during the transition, the profit allocation can recognise the contribution and needs of each generation to allow independent financial growth
- Transitioning a viable business to the next generation is the next step. For broadacre farms, business scale sufficient to achieve farm income of \$900,000 per on-farm family is a starting point to determine business viability
- Business health check guidelines can help to determine what business income, costs, debt and assets are required for a viable transition to the next generation

## Transitioning a financially viable farm business to the next generation

**Please note: In the context of this fact sheet, generational transition, generational transfer and succession planning refer to the same process and the terms can be used interchangeably.**

### Introduction

Generational transfer can culminate in the immediate withdrawal and retirement of the parents, or it can start well before the older generation is ready to retire. A transition over 10 to 15 years is often beneficial.

Generational transfer involves the transfer of management responsibility, the transfer of asset ownership and, sometimes, the sharing of farming assets and profits to ensure the transfer is feasible and viable.

The financial implications and framework around the generational transfer require clear and rational

analysis early in the process to ensure a reasonable, fair and viable transition is achieved. This factsheet provides a framework to estimate and discuss the financial realities that underpin a viable and successful transition of a farming business to the next generation.

### Transition of management

Transition of management responsibilities should be undertaken in stages, starting with the technical decisions and then moving through the tactical, strategic, supervisory and financial control. This ensures the skills at each level can

be developed and cemented before additional responsibilities are transferred between generations (Errington, 2002).

Transition of management and profits can begin while both generations are still both actively involved in the business. If both generations are farming together, careful consideration of profit allocation for independent wealth creation is important.

Alternatively, during the transition period, the next generation may appreciate the opportunity to farm independently. Here, parents can assist by providing access to farming land and capital support through the use of machinery or land at discounted rental rates. Future land acquisitions and machinery upgrades can be directed through to the next generation so that they can commence equity growth.

For either option (farming together or alongside), the parents can allocate their share of profits to independent investments for their financial security and for their off-farm children's inheritance.

## Transition of assets

Over the past 10 years the net asset value (asset value minus debt value) of many Australian broadacre farming businesses has increased four-fold, largely driven by similar-sized increases in farmland prices. In this environment, to get started in farming, the next generation needs access to a land base valued at close to \$6 million. The land base can be owned outright; however, it often includes land owned by family, or external owners accessed through lease or share-farm agreements.

## Net asset value of family farms

AgProfit tracked a continuous group of broadacre family farms in the Wimmera–Mallee region from 2013 to 2023. Over that period, the average net assets of the group increased more than 400 per cent due to a combination of farm expansion and rising land, water and machinery values (Table 1).

The group now operates with average net farm assets of close to \$30 million.

**Table 1: Shift in average net assets of Wimmera–Mallee broadacre farms (from 2013 to 2023).**

|                   | 2013<br>\$m | 2023<br>\$m | 10 year<br>change<br>\$m |
|-------------------|-------------|-------------|--------------------------|
| Farm assets       | \$6.8       | \$34.8      | \$28.0                   |
| Total liabilities | \$1.8       | \$5.0       | \$3.2                    |
| Net farm assets   | \$5.0       | \$29.8      | \$24.8                   |

Source: AgProfit™ farm data

This substantial growth in net asset value is helpful for the balance sheet and provides a larger asset pool for succession planning. However, when considering farm generational transfer this steadily increasing net asset value can lead to concerns as to what is a 'fair' allocation to both the on-farm and off-farm children.

If it is the older generation's aspiration to transfer a 'viable' farming business to the next generation of on-farm family members, it is important that all those involved (parents, on-farm and off-farm children) understand what magnitude of financial and business components are required to be a financially viable farming business. An understanding of these figures can help all involved to understand the decisions around asset transition.

The current business should also have the capacity to not only be viable for the next generation but also provide sufficient equity for the parents' financial security in retirement.

## Business viability

As a starting point, to validate the financial viability of the current business, industry business viability indicators can help review current performance and provide a useful communication tool for all family members to explore realistic and viable options for generational transition.

Key measures of financial viability include profit for debt servicing and asset availability as security.

Suggested key indicators of business viability are listed in Table 2.

**Table 2: Indicators and guidelines of business viability.**

| Indicator   | Guideline             |
|---|-----------------------|
| Debt to land asset ratio  | Less than 40 per cent |
| Total farm income as percentage of asset value (assets include land and water under management and machinery) | 10 to 15 per cent     |
| Profit as percentage of total farm income   | 6 to 10 per cent      |
| Interest (and land rent) as percentage of total farm income   | Less than 15 per cent |

Source: ORM data

## A viable scale for the next generation – a scenario

The worked analysis shown below builds a scenario exploring what income and asset levels are required to support family members within a 'typical' farming business. This is a good talking point for succession discussions.

### SCENARIO

If the family's goal is to have \$200,000 available for living, school fees, tax and debt repayment then the guidelines, as provided in Table 3 and Table 4, can be applied to determine the total farm income and the asset value necessary to sustain a family unit at their targeted income.

Based on the AgProfit™ guidelines detailed in Table 3, we know that typically, labour costs and operating profit represent 15 and eight per cent of total farm income, respectively. When these two values are combined this represents 23 per cent of the total farm income. This is the portion of income available for living.

- For this scenario, total farm income of \$900,000 is required to meet the family goal of \$200,000 available for living, school fees, tax and debt repayment.
- Tables 3 and 4 on page 3 detail how this is validated.

**Table 3: Typical industry cost guidelines (AgProfit™) used for the calculations detailed in Table 4 below.**

| Total costs as percentage of total farm income (TFI) are:   |             |
|---|-------------|
| • Overheads (rates, insurance, professional fees)   | 8 per cent  |
| • Farm inputs (fertiliser and sprays, seed, etc.)   | 30 per cent |
| • Machinery (fuel, repairs, contracting, capital replacement)   | 28 per cent |
| • Finance (interest, bank fees and rent)  | 12 per cent |
| • Labour (owner's time and casual employees)  | 15 per cent |
| Operating profit as percentage of TFI   |             |
|   | 8 per cent  |
| NB. Guidelines can vary across regions and farming systems. Further information is available through the AgProfit™ website (agprofit.com.au). |             |

Source: AgProfit™ farm data

**Table 4: Typical break-up of \$900,000 total farm income to achieve \$200,000 available family income.**

|                                    |             |
|------------------------------------|-------------|
| Total farm income (TFI)            | \$900,000   |
| Less expenses                      |             |
| Farm input costs (30 per cent TFI) | \$270,000   |
| Machinery (28 per cent TFI)        | \$252,000   |
| Finance (11 per cent TFI)          | \$105,000** |
| Labour (15 per cent TFI)           | \$126,000*  |
| Overheads (8 per cent TFI)         | \$72,000    |
| Operating profit (8 per cent TFI)  | \$75,000*   |

Source: ORM data

\* \$126,000 Labour and \$75,000 operating profit combine to provide \$201,000 available income.

\*\* Financing costs of \$105,000 indicate debt load should not exceed \$1,750,000 based on an indicative bank interest rate of 6 per cent.

## What farm scale is needed to generate \$200,000 of available family income?

- Total farm income (TFI) is typically 10 to 15 per cent of asset value (land, water, livestock and machinery) (Table 2).
- In this example, a TFI of \$900,000, would require a total asset value of \$6,900,000.
- The typical machinery asset value guideline suggests a 1:1 ratio of machinery to annual total farm income. For this example, this ratio places total machinery value at \$900,000.
- This suggests a land asset market value of approximately \$6,000,000 (dryland, broadacre farm) is required.

This scenario analysis indicates that, typically, a total farm income of \$900,000 and a land asset value of approximately \$6 million are required to support the next generation and provide opportunity for them to grow.

## Contributions from the parents

The worked example illustrated in Table 4 confirms that the next generation requires access to a significant asset if they are to achieve a viable scale. Options for how this can be achieved in this example are:

- 1 Next generation lease some of the parents' land to the value of up to \$6 million with a subsidised land rental.
- 2 Land valued up to \$6 million be transferred from the parents to the on-farm child/children with a payment to the parents of \$1,750,000. This is equivalent to the appropriate debt loading according to viability guidelines (Table 4\*\*). Interest on this amount provides income for the parents and can be quarantined as a future asset for any off-farm children.
- 3 Lease or purchase new land with some equity contributed by the parents. If leasing then the lease payment is part of the finance cost, that is \$105,000 (finance cost is the total of interest and land lease payments).
- 4 Combinations of the above.

## Conclusion

There are many variations on how the next generation can transition into a viable farming business. The best option for each business is dependent on first, the needs and preferences of the parents, and second, those of the next generation – in that order.

Generational transition in a family farm business is about understanding the needs and preferences of the people involved, including those in the business and those outside the business (that is, off-farm family members).

The parents' preference for asset ownership should determine whether land is transferred, or ownership is retained by the parents. If land ownership is retained, then the commencement of financial independence for the next generation can be through the future growth of the family business. For example, future land purchases can be in the name of the next generation with debt repaid through joint business profits.

Current business health check guidelines and indicators can assist in understanding the magnitude of the financial factors involved in developing the most appropriate process and timelines to facilitate viable generational transfer.

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## FREQUENTLY ASKED QUESTIONS

### When do we start transferring management responsibility to the next generation?

The next generation can start taking responsibility for specific areas within the business as soon as they return to the business. However, it's often good to give them two to three years to settle in and find the areas of the business in which they have the most interest.

### Is it OK to retain ownership of the current land, or do I need to transfer the land before I retire?

Transfer of land is the last step in the succession process. It is up to the parents as to when and if they transfer the land. If retaining the land, then they may need to be guarantors for future expansion undertaken by the next generation. Alternatively, if they intend to receive the aged pension then they may prefer to transfer the land. Accountants and legal professionals should be engaged well in advance of any decision on the transfer of assets, to assist with tax and legal obligations including, for example, stamp duty on transfers of land and capital gains tax, as two examples.

### Could some of the income requirement for the family be substituted with 'off-farm' income from a spouse to assist with transitioning the farming assets?

Off-farm income can reduce reliance on the farm property to support the family's needs. This can have an impact in regard to the size and value of the asset base required. The long-term sustainability of off-farm income could enable the acquisition of larger assets, as the farming operation's capacity to service increased debt is enhanced by the supplemental income covering family living expenses.

## USEFUL RESOURCES

**GRDC Fact Sheet – Succession Planning**,  
[grdc.com.au/resources-and-publications/all-publications/factsheets/2010/10/succession-planning-fact-sheet](http://grdc.com.au/resources-and-publications/all-publications/factsheets/2010/10/succession-planning-fact-sheet)

**Farm Business Models GrowNotes™**,  
[grdc.com.au/resources-and-publications/grownotes/technical-manuals/farm-business-models](http://grdc.com.au/resources-and-publications/grownotes/technical-manuals/farm-business-models)

## MORE INFORMATION

**ORM Pty Ltd**  
[orm.com.au](http://orm.com.au)

## REFERENCES

Errington, A. 2002 'Handing Over the Reins: A Comparative Study of Intergenerational Farm Transfers in England, France and Canada,' *10th European Association of Agricultural Economists (EAAE) International Congress*. Zaragoza, Spain, 28-31 August.

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