

COMPENSATION

Discussions around compensation commonly come up during transition because family members' situations usually are changing as part of the transition plan. As discussed in previous sections, the retiring generation may want to increase their compensation depending on their retirement plans. The succeeding generation may now be exploring the option of giving up an off-farm job — depending on what they will get paid on the farm. Now is a good time to put some structure to the compensation individuals are going to receive.

Designing a compensation plan for a family farm brings up the following questions:

- What is fair pay among family members?
- How do I determine a fair wage for family members and non-family employees?
- How should shareholders be paid?
- How can we resolve disputes over pay?
- How should family assets be handled?

The issue of fairness is difficult because each of us has a different idea of what is fair. A farm operating under a business-first philosophy would say that fair is being paid based on the job that is to be done — at the going market rate for the job. Hiring is based on the skills, experience and initiative that an individual brings to the job.

A farm operating with a family-first approach would say that all members are a part of the family and therefore should be paid the same regardless of the job they are doing. Another interpretation of fair is if one of the children has not done as well as the others, it may seem fair to provide equal compensation to him or her so they can enjoy the same lifestyle as others in the family.

Money can go from the family farm business to individual family members in a variety of ways. There are dividends, wages, bonuses, merit increases, loans, gifts (housing, school, vehicles,) training allowances, perks (vehicles, vacations, trips, business and personal expense allowances), ownership and equity gains in land, inheritance, trusts and bequests.

Why is this relevant?

A well designed compensation system that makes sense and is understood by everybody accomplishes the following:

- maintains control and structure over pay
- keeps the business on track
- promotes individual development
- provides a clear statement about work ethics and values
- encourages individuals to accept financial responsibility for themselves
- provides a clear understanding about the value of different jobs
- promotes trust
- motivates individuals to perform well
- distinguishes between compensation and gifts

The compensation policy can include specific suggestions that pertain to the transition plan and its implementation.

How will this help transition planning?

- Talking about compensation (money) can help to lessen the potential for conflict.
- A compensation policy that is shared with farming and non-farming family members helps to keep the non-farming members current with the business of the farm.
- It can help to reduce the potential for hard feelings between arms-length employees and family members who may be doing similar jobs but getting paid differently. This is done by developing a more appropriate way of compensating arms-length employees and family members.
- Once developed, it becomes a basis to determine compensation when other family members decided to return to the farm.

Instructions

The compensation exercise is to be completed by everyone together.

1. Go through the following list of things you can consider as you create a family compensation philosophy. Record the answers to the questions on a separate piece of paper. Remember that you can refer to the different forms of compensation listed above.
 - Will wages be paid?
 - What will the wage rates be based on? (market value, equal wages for all, perception of need, other)
 - What criteria will be by used to increase base rates? (inflation, cost of living, company performance, need, merit)
 - What will the timing be for wage increases?

- Will dividends be paid? **NOTE:** *Even if your farm is unincorporated, the concept of dividends can still be applied.*
 - What will dividends be based upon? (farm equity growth, net income performance)
 - Will bonuses be paid?
 - If so, what will bonuses be based upon? (seasonal, ex: Christmas, harvest etc., company performance, individual performance, reaching training or education milestones)
 - What will be the philosophy be around gifts or entitlements?
 - Examples: All children will receive a vehicle on their 17th birthday. All children will receive four years of paid education. The family will go on one annual paid vacation. All children will receive a set amount of money towards their first home down payment. Interest free loans will be provided.
 - Will business perks be provided?
 - What perks will be provided? (phones, utilities, vehicles, fuel, business trips, housing etc.) **NOTE:** *Be sure to check with your accountant regarding the tax implications of the business perks you are considering.*
 - Will there be limits on perks?
 - Will training be part of the compensation plan?
 - Will all members have equal access to training?
 - What will be the limits to time and money spent on training?
 - Will training be mandatory or included in merit increases or bonuses?
 - Will ownership of assets or shares of the company be part of the compensation plan?
 - When will members become owners?
 - How will ownership amounts be decided and awarded?
 - Will assets be transferred to individuals?
 - Will the farm make payments on personal assets?
 - Will inheritances or bequests be part of the compensation plan?
 - What will be the criteria to earn an inheritance or bequest?
2. Create and write down a compensation philosophy according to the sample template (an example is shown below).
 3. Store the document for future reference.



EXAMPLE

Sample Farms Ltd. Compensation Philosophy

For Owners

- After five years of work on the farm, family employees can take their share of bonuses, wage increases and increases in partnership interest (or common shares of a corporation).
- Family employees with less than five years can accumulate their bonuses and merit pay.
- All owners and their spouses will meet once or twice a year. All persons attending will be reimbursed for reasonable travel expenses and paid a set per diem amount.
- All owners will receive a minimum amount per year.
- Dividends will be paid in the amount of two per cent of earnings.

For Family

- Tuition and student expenses will be paid.
- Loans for houses and vehicles will be available at attractive interest rates, as per management approval.
- Gifts will be given independent of the business.

For Family Employees

- Wages will be objectively determined.
- Wages will be somewhat conservative (ex: 75 per cent of market value) given family ownership and the variability of the farm economy.
- Wages will be determined based on the size of the job, responsibility, relevant training and experience, and working conditions.
- Wage increases and vacations will be based on years of experience, seniority and cost of living.
- Annual merit pay will be awarded. This will be based on jointly agreed-upon goals that will be determined at an annual performance planning meeting.

How does this apply?

The compensation philosophy should be shared with all family members involved in the business or those who may be looking to become involved in the business. Compensation is an area that can cause conflict if family members feel they are not being treated fairly or someone is not pulling their weight. It is important to review the compensation policy at least annually:

- to keep it current
- to address any issues with compensation that family members have
- to avoid conflict over what members are getting paid



PLANNING POINTERS:

- Consider using an external facilitator if you are concerned about the potential for conflict. Money and emotion are closely tied. Discussions about money easily trigger disagreement and conflict.
- Review the compensation policy annually and make the appropriate adjustments.
- Try to be fair and realistic about compensation — both from an underpaying and overpaying perspective.



WHAT TO WATCH FOR:

- Do not try to maintain control by tightly hanging onto the cheque book.
- Do not pay someone more than what the task they are doing is worth. If the employee (or family member) has been around for a long time, find other ways to appropriately reward them for their loyalty.



EXERCISE: Go to the forms appendix at the back of this guide for a blank copy of the Compensation exercise on page 289.

Next steps

Congratulations on completing this topic. You are now a step closer to having a transition plan for your farm. Please proceed to the next topic area on your Transition Plan, but don't forget to add any assigned tasks that were generated by working through this topic.

Compensation

Compensation Philosophy

For Owners

For Family

For Family Employees
