

## MAKING A WHOLE-HERD BUYOUT BID: THINGS TO CONSIDER

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1. First consider what is most important to you, to other family members as individuals, to you as a family?
  - Cash income to pay for .....
  - Leisure time for.....
  - Occupation (dairy farmer, farmer, off-farm work)
  - Holding on to the family farm
  - Passing the farm along to children
  - Financial security in retirement
  - Pride and status in community
  
2. What financial shape is your business in? Can you survive? If so, is that what you want?
  - Net income for the last 3 years and projections for the next 3
  - Changes in debts and assets owned over the last 3 years from balance sheets and current statement of assets and liabilities
  - Cash flow summary for the last 3 years and projections for the next 3, including business operating income and expenses, capital purchases and sales, new loans and loan payments, family living and non-farm income.
  - Can the financial picture be improved by increased efficiency, sale of farm assets, debt restructuring, off-farm income, bankruptcy?
  
3. What are your alternatives if you stop producing milk? Which is the best alternative for you?
  - Expected net income from other farming alternatives
  - What off-farm jobs are available? What jobs are you qualified for? What do they pay? What is available for other family members?
  - What farm assets can be sold for how much (net of sales commission and taxes)? Will this pay off the farm debt? Will there be money left over to invest? Where will it be invested and at what rate of return?
  
4. What are you planning to do or likely to do if you do not participate in the buyout program? Continue dairy farming or sell out anyway? If you plan to sell out anyway how soon would you sell?
  
5. What economic costs would you bear by participating in the herd buyout?

- Loss of income if cattle are sold for slaughter not for dairy purposes, and expected losses (or gains) from changes in cattle prices if you would otherwise sell at a different time.
- Loss (or gain) in expected net income because net income from dairying is higher (or lower) than net income from the next best alternative, including cash income and non-cash earnings from land appreciation etc.
- Start-up costs if you plan to re-enter dairying, including the cost of cattle and net income losses during the rebuilding period.

#### 6. Bidding strategy.

- What is the breakeven bid to cover the relevant economic costs of entering the program compared to the best alternative. Anything above the breakeven bid is financially beneficial.
- There is very little information to help a producer guess the upper limit on a bid and still have it accepted—we are shooting in the dark.
- Look at your circumstances and figure the effects of different bids. How large a bid would prevent bankruptcy? Save the family home and personal possessions? Clear the debt on the farm? etc. A clear understanding of the impact of different bids helps to focus on gains and losses from submitting a bid of a certain amount, which is a gamble.
- Avoid even numbers, Stores use “odd pricing” such as \$9.99 not \$10.00 and the same approach might make a bid that is close to the maximum more competitive.

#### 7. The tax consequences of participating in a buyout could be significant. Consult your tax counselor or accountant on the tax consequences of a successful bid and the choice of a payment option. The tax consequences of a successful bid and the choice of a payment option.

- Discuss how the CWT payments will be taxed, i.e., ordinary income or compensation for the loss of value from the sale of cows (business property).
- Income from the sale of raised cows and heifers over 2 years old is eligible for capital gain treatment.
- Income from the sale of purchased cows, machinery and equipment might be liable for depreciation recapture or capital gains treatment depending on the tax basis (cost).
- If land is sold for more than the basis (cost) the difference is taxable as capital gains.
- Sale of young stock and feed, rent received, are taxed as ordinary income.
- Carryover of investment tax credit and net operating losses may be available to offset part or all of the tax liability.
- Income averaging and installment sales of non-dairy assets might also reduce total tax liability.

#### 8. Consult lien holders and major creditors before submitting a bid if secured property will be sold. Also discuss how the sale proceeds and program payments are to be used. Any remaining debts may need to be restructured and the payments rescheduled to fit a different income pattern.