

Structural change and farm handover

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Abstract - The ongoing structural change in agriculture is still an issue. Politician and society fear an encroachment of wilderness. Further, they want to have a certain degree of self-sufficiency for specific foodstuff and they want to prevent a depopulation of rural areas. Congruously, we see a sophisticated framework encouraging the continuation of farming, including the handover of farms from one generation to the next one, i.e. from elder farmers to their successor. Related to an upcoming handover, more than in any other economic sector, the regulation emphasizes the conservation of vital operational units. In enforcing the conservation of vital operational units, i.e. farms, in Germany the regulation even accepts uneven inheritances. But the promotion of uneven inheritances implements unintentional incentives to continue even with those farms which realise small losses. In some of the neighbouring counties of Germany the same problem exists, in other neighbouring countries the different regulation sidesteps the unintended effect. Due to the sidestep, uneconomical farms give up and the structural change in agriculture is higher; therefore agriculture realizes higher efficiency gains.

INTRODUCTION

The ongoing structural change in agriculture is still an issue. Politician and society fear an encroachment of wilderness. Further, they want to have a certain degree of self-sufficiency for specific foodstuff and they want to prevent a depopulation of rural areas (Bundesministerium für Ernährung, Landwirtschaft und Verbraucherschutz, 2009: Nationaler Strategieplan der Bundesrepublik Deutschland für die Entwicklung ländlicher Räume 2007-2013; Williams, Farrington, 2006). Congruously, we see a sophisticated framework encouraging the continuation of farming, including the handover of farms from one generation to the next one, i.e. from elder farmers to their successor (Zech, 2004). Related to an upcoming handover, more than in any other economic sector, the regulation emphasizes the conservation of vital operational units (Doll et al., 2001; Köhne, 1995; Mann, 2009; Senti, 2006). In enforcing the conservation of vital operational units, i.e. farms, in Germany the regulation even accepts uneven inheritances (Bonefeld, Deiniger, 2004; Tietje, 2003). But the promotion of uneven inheritances implements unintentional incentives to continue even with those farms which realise small losses (Doll et al., 2001, Köhne, 1995; note also Peyerl, Bahrs, 2007). In some of the neighbouring counties of Germany the

same problem exists, in other neighbouring countries the different regulation sidesteps the unintended effect (Bonefeld, Deiniger, 2004. Senti (2006) points out that the practised market value assessment in France had no relevant negative influence on farmers financial situation.). Due to the sidestep, uneconomical farms give up and the structural change in agriculture is higher; therefore agriculture realizes higher efficiency gains.

The model at hand analyses the decision concerning a potential farm handover. Especially in sideline farms, where emotional relatedness to agriculture has already decreased, the economic calculation concerning to the long run stipulates whether to go on with farming or whether to opt out of agriculture. The calculation takes essential tax regulations into account, which – in Germany - strongly favour the conservation of vital farms units, inter alia through promoting an uneven heritance (Bonefeld, Deiniger, 2004). In contrast, the tax regulation in - e.g. - Denmark differs even though vital farms are promoted too, in Denmark. But the regulation in Denmark does not entrap to continue with uneconomical farms. It utilizes a different view on estate and wealth.

Coming back to the German regulation, the model analyses the limit up which losses are accepted and do not prevent from going on with farming. Further, the impact of uneven inheritance will be discovered analytically. The inclusion of additional tax incentives into the calculation is discussed. Ditto, the inclusion of the reserved property of the ceding generation is discussed.

FUTURE BEQUEATHERS AND SUCCESSORS DECISION

The micro economic model compares the long run payoff of different decision alternatives, taking into account national law and especially national tax law, and first of all the inheritance tax law and the income tax law. As the law takes the capitalized earnings value as a reference (in terms of taxable base) in case of a farm handover to one and only one successor, the future bequeather of a large farm has a strong incentive to nominate one successor. In case of potential additional successors, the farm handover becomes a decision of long run family property preservation (which is comparable to bequeather's individual efficiency) versus equal treatment among the heirs (which is comparable to fairness). But this unlovely trade-off is only one of the problems in farm handover.

As the closure of farming activity and the conversion of farm property into private property (in preparation of an even inheritance) is accompanied by

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larger tax payment due to referring to the market value of the farm instead of referring to the capitalized earnings value, the exit from farming as well as the even inheritance imply a relevant loss of family property. The omission of this loss may justify accepting small yearly losses from an ongoing farming activity by a successor.

Further, in an uncertain future legal environment, there might emerge an option of more favourable conditions concerning conversion of farm property in the course of an upcoming inheritances or farm handover. Whenever there is uncertainty about future payoffs of an irreversible 0-1 decision, there is an option value for delaying the decision. The example of the amendments of the inheritance laws in Austria as well as in Germany point up this issue.

DISCUSSION

The model allows to structure countervailing effects of yearly losses and special non-recurring taxes. The analysed trade-off is induced through the special betterment of capital bounded to farming compared to other forms of capital. It might induce inefficiency in agriculture and an artificial slow down in structural change. Therefore, it may hinder neighbouring farms to grow and maybe to stay competitive. Thus, the second order effect may work against the first order effect, the intended preservation of vital operational farming units. Insofar there is a parallel to the model of Travernier and Li (1995). Farmers are trapped through the special relief by use-value assessment, respective capitalized earnings value assessment.

Further, through the option of changing legal frames, e.g. favourable relieves for the conversion of farming property into private property, there is an additional incentive to delay the conversion. This affects not only efficiency in agriculture; it also affects fairness in inheritances in agriculture. An even treatment of all heirs becomes delayed, too.

Therewith we are back to the actual conditions; the legal frame forces farmers to weigh up efficiency in property conservation and fairness amongst all heirs. Unfairness may induce stress between heirs and legal actions especially in those cases, where the assessment practice is neck or nothing, e.g. for farms at the rural-urban fringe, where land market values are high (Haimböck, 2001).

OUTLOOK

The model applied the former regulation and inheritance law, as it was crucial for the development of the current agricultural structure. More than a year ago, regulation changed in Austria as well as in Germany. The effect should be analysed in order to evaluate future development. Further, the amendment was broadly discussed in advance. Farmers are aware of the uncertain future legal environment. How much does the uncertainty affect their decision? Is the economic issue crucial for their handover decision, respectively for the decision of a potential successor to go on with farming? How much do emotional issues count for? What turns the balance – emotional relatedness or economic calculation?

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