

RIGHTRISK™

RIGHTRISK NEWS

DATES TO REMEMBER

Spring-planted crops sales deadline:
- March 15, 2019

Noninsured Crop Disaster Assistance Program (NAP)
Deadline for springseeded forage and all other crops
- April 1, 2019

For more information see:
<http://www.rma.usda.gov>
<http://www.fsa.usda.gov>

Which Business Entity is Best?

Historically, farms and ranches were operated as sole proprietorships. The land, machinery, livestock, and other assets were owned and operated by an individual or by close family members. Likewise, the operators were personally responsible for all debt and financial obligations owed by the business. The farmer or rancher was the business, and the business was the farmer or rancher. However, there are a number of other entities that may better meet the needs of today's farm/ranch business. A few of the more commonly-used business entities include: sole proprietorship, partnership, corporation, and limited liability company (LLC).

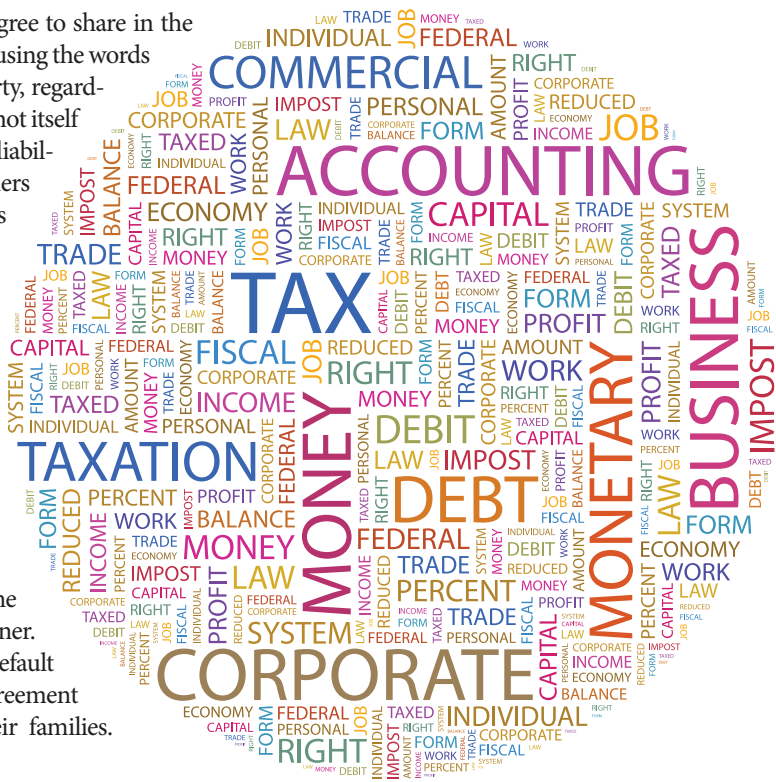
Business owners should determine the goals of and needs for the business and its assets before a decision is made as to the legal entity under which to operate. Is there interest in maximizing management flexibility, protecting owner liability, managing income tax liability, minimizing formation and ongoing administration costs, or easing transition of ownership to new or other owners?

Sole Proprietorship – is the simplest, most common form of business ownership. An individual, or in some cases a husband and wife, owns all the assets, is responsible for all liabilities, and has full control of management and operation. A sole proprietorship generally has no annual filing requirements with the Secretary of State in the state where it operates.

A sole proprietorship has no separate tax status. It is recognized by the Internal Revenue Service as an extension of the owner. Thus, the owner reports all income and expenses on his or her personal tax return. In addition, there are no specific rules nor special strategies for transferring ownership of assets or control of the business under a sole proprietorship. The business owner may gift or sell ownership of the assets as a part of a succession plan. Also, the farm or ranch owner should include all property in his/her individual estate plan.

Partnership – is an association of two or more individuals who agree to share in the profits or losses of a business. A partnership can be formed without using the words “partner” or “partnership.” However, the joint ownership of property, regardless of how the owner's names are listed on the title of an asset, does not itself establish a partnership. There are various types of partnerships with liability being the key point of difference. In a general partnership, partners manage the company and assume responsibility for the partnership's debts and other obligations.

A partnership does not pay tax on its income but “passes through” any profits or losses to the individual partners. A partnership must compute and report its income, as well as indicate to each partner (on a IRS Schedule K-1 form) his or her share of partnership income, deductions, and tax credits. In turn, each partner is required to report profits from the partnership on his or her individual tax return. A partnership should be documented by a written agreement that specifies contributions made by each partner and how profits or losses are to be divided. Further, the agreement serves as a written record of the business arrangement in the event of future disputes, imperfect memories, or the death of a partner. It can help reduce the risk that partners will be surprised by any default rules in existing partnership statutes. Also, a written partnership agreement should enhance communications between the partners and their families.



How Much Risk is Right for You?



Limited Partnership – has both general partners who own and operate the business and assume liability for the partnership, as well as limited partners who serve only as investors. A limited partnership has at least one general partner and at least one limited partner. Management of a limited partnership is vested in the general partners. Unless the partners agree otherwise, profits and losses of a limited partnership are presumed to be allocated on the basis of the value of the contributions made by each partner rather than equally as with a general partnership.

Another form of limited partnership is the **limited liability partnership (LLP)**. An LLP is a general partnership where all partners have limited liability in regard to the partnership's debts. A minority of states have also adopted statutes which expressly authorize the formation of **limited liability limited partnerships (LLLLPs)**. An LLLP is a limited partnership where the general partner has the same protections against personal liability that a general partner has in a regular LLP.

Corporation (C Corp) – is an independent legal entity created to conduct business. Corporations are formed under the laws of each state with their own set of regulations. A corporation is taxed and can be held legally liable for its actions. Further, corporations generally are required to use the accrual method of accounting. A corporation's debt is not considered that of its owners. A corporation also can retain some of its profits, without the owner paying tax on them. Corporations continue indefinitely, even if one of the shareholders dies, sells the shares, or becomes disabled.

An extra cost associated with a corporation arises where the owners pay a "double tax" on business earnings. Not only are corporations subject to corporate income tax at both the federal and state levels, but any earnings distributed to shareholders in the form of dividends are taxed at individual tax rates on their personal income tax returns.

S Corporation – is a corporation that provides business owners with the liability protection of a corporation while passing income and losses through to shareholders. Thus, there is no double taxation. S corporations are subject to many of the same requirements as C Corps. They must file articles of incorporation, hold directors and shareholders meetings, keep corporate minutes, and allow shareholders to vote on major corporate decisions. The legal and accounting costs of setting up an S corporation are similar to those of a standard corporation. Also, S corporations can only issue common stock.

Limited Liability Company (LLC) – is a hybrid form of partnership which allows owners to take advantage of the benefits of both the corporation and partnership forms of business. An owner (called a "member") can be a person, partnership, corporation, or a trust (in some cases). All members are allowed full participatory roles in the business operations. The profits and losses are typically passed through to owners without taxation of the business itself, while owners are shielded from personal liability. The risk of owners is limited to the amount of capital paid into the business. An advantage of an LLC is that profits and losses do not need to be distributed in proportion to the owner's investment. An LLC must file articles of organization with the Secretary of State in the state where the LLC does business and some states also require an operating agreement.

There are several reasons to select one form of business organization over another. Farm or ranch owners should first determine their needs and objectives and then match those needs with the advantages and disadvantages of each form of business organization. Counsel from competent legal and accounting professionals should be sought before making a choice, as rules are always changing and the details associated with each form of ownership are complex. It is critical for both short term success and long-term sustainability that the business owner select a structure that best fits the goals of both the owner and the owner's family.



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RightRisk News is brought to you by the RightRisk Team

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How much risk is right for you and your operation?

