Beginning Farm Business Arrangements

AAE 320

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Goal

• To present some “words of wisdom” on how to start working with an older generation to become a farmer
• No right or wrong way, just some general guidelines
Beginning Arrangements

- Farmers have business life cycles and each farmer is different
- Some important issues
  - 1) Level of ability and objectives of the established farmer
  - 2) Beginning farmer’s ability and timing relative to the established farmer’s life cycle
  - 3) Treatment and expectations of the beginning farmer by the established farmer
Recommended Phases

• 1\textsuperscript{st} Employee-Employer Agreement
  – Testing phase

• 2\textsuperscript{nd} Operating Agreement
  – Formal business arrangements [trusted lawyer]

• Communication important

• Eventually likely have to put things in writing: way to clarify details, address things you all may not have thought of, etc. [trusted lawyer]
1st Employee-Employer Agreement

• Compensation
  – Cash
  – Wage and income share
  – Incentives
  – Bonus payments
  – Fringe benefits
  – Commodities (not subject to SE tax)
2nd Operating Agreement

• Beginning operator
  – May furnish some personal property such as livestock or machinery
  – May provide some management as well as labor

• Established operator
  – Provides land
  – Capital/collateral
  – Management

• Early on, may just be oral, but if it grows, arrangement may need to be put into writing, then you need a trusted lawyer
Operating Agreement

• Agreements should cover topics such as:
  – Job responsibilities
  – Contributions of assets
  – Distributions of income
  – Method of settling disputes
  – Dissolution of the agreement
  – Short-term (1-2 years) with clear end date specified by which to renegotiate
Joint Operating Agreement

- Operators are sole proprietors
- Each contributes assets, management & labor
- Income is shared based on inputs
- Each pays expenses of their assets
- Operating expenses are split
Joint Operating Agreement

- Complete inventory should be taken at start
- Sale triggers recognition of gain, so avoid
- Could be transferred by gift
- Could allocate income to pay for inventory
- Could repay at end of agreement
Enterprise Agreement

• Type of Operating Agreement: specify which farm enterprise(s) are managed by whom
  – Young farmer may run the dairy (owns cows, not buildings)
  – Older farmer (owns land) runs grain and forage production and sells to the young farmer, pays young farmer to help during planting and harvest

• Beginning operator’s income is all from one enterprise
  – Beginning farmer takes over an enterprise
  – Dairy, crop production, grain marketing, ...

• Labor for other enterprises may be a source of conflict
  – Less time for other activities used to do
Total Farm Operating Agreement

• Other main type of Operating Agreement
• All income and operating expenses are split
• Beginning operator slowly acquires more assets over time via a transition process
Leasing

• Cash leases
• Crop share leases
  – Share inputs and/or outputs
  – Variable rate based on production
• Livestock share leases
Leasing

• One farm enterprise can lease assets from other parts of the farm or other farmers/owners
• Allows beginning farmer use of large capital items when has only a little capital
  – Does not have to be the older generation
• Short or long term
• Land, buildings, machinery, livestock
• Leases for more than a year must be in writing
• 90 day notice required to terminate a year-to-year agricultural lease
Leasing Other Assets

• Leasing a building: from builder or bank
  – An alternative to financing
• Leasing from a neighbor
  – Clarify about cost of maintenance and repairs
• Livestock leasing
  – From leasing company
  – From retiring farmer
  – Advantages for beginning farmer and retiring farmer
  – Clarify maintenance and care expectations
Summary

• Provided some “words of wisdom” on how to start working with an older generation to become a farmer
• No right or wrong way to do it, each family has to find a way that works for it
  – Communication is key
  – Remain flexible & renegotiate as people age
  – Not all families can work together