Business Structures Information Sheet

The way a farm or ranch business is legally structured can affect farm transfer. So it is important to understand the different kinds of structures and what protections they may or may not provide. This is especially important if the transfer includes some or all of the farm or ranch business, along with land and other real estate assets.

There are four main types of business structure: **Sole proprietorships**, **partnerships, limited liability companies**, and **corporations** including cooperatives and nonprofits. This information sheet briefly summarizes what they are.

Sole Proprietorship

In sole proprietorships, the business is owned and run by one person. Legally there is no difference between the owner and the business. They are pass-through or flow-through entities, which means that business income is treated as the owner's income and is reported on the owner's personal tax return.

Sole proprietorships are the simplest and cheapest type of business to create. But they have unlimited liability, which means they do not offer the owner any legal protections for personal assets. This leaves the owner solely responsible for all business activity, including lawsuits and debt, leaving the owner's personal assets—even their home—at risk. Further, because their assets are undivided, it may be more difficult for an owner to transfer individual assets to different people. This can be challenging and time consuming if the owner wants to create a transfer plan that involves multiple successors

Partnership

Partnerships are the easiest way to allow two or more people to be in business together. They also are pass through entities. In **General Partnerships**, owners have equal power and share profits and losses. In **Limited Partnerships**, one main partner may play the primary role managing the business and daily operations. Typically, profits and losses are shared between partners based on the amount of their involvement in the business.

In a partnership, assets can be sold, gifted, or passed through an estate over time. Stretching out the transfer gradually can spread out income and reduce taxes, lowering the capital needs of the incoming producer and making it possible for them to acquire assets over time.

Limited Liability Company (LLC)

LLCs are also pass through entities but unlike sole proprietorships and partnerships, the business entity is separate from its owners. LLCs are fairly easy to create and provide limited liability so they protect owners from lawsuits and debt. LLCs often are the structure of choice for a farm or ranch business because they offer protections but are flexible and a good way to transfer both management and ownership.

Corporations

Corporations are organizations that are a separate legal entity and distinct from their owners. Authorized by the state and recognized by law to act as a single entity, they are owned by stockholders—or shareholders—who share in businesses' profits and losses. Because they are separate from their owners, they are taxed separately. Owners are not personally liable for company debt, and their personal assets are not at risk if the company fails or is sued.

A corporate structure can facilitate the process of transferring a farm business to the next generation. Shares can be sold, gifted, or passed through an estate as, eliminating the need to transfer separate, individual assets and spreading out income (and taxes). This makes it easier for the incoming producer to acquire assets over time, reducing their need for large amounts of capital

There are five types of corporations. **C Corps** are usually large corporations, while **S Corps** only allow up to 100 shareholders and provide for pass through income, so are a common option for farm or ranch businesses. **Cooperatives** are owned and operated by the employees or people who use the product or service the business produces. They are managed equally by the owners and profits are distributed equally among all members. Nonprofit organizations are considered corporations because they file articles of incorporation in the state where they are registered. But they are considered non-business entities because their purpose is to serve a charitable mission or cause, not to earn profit. By claiming 501(c) status with the IRS, they are exempt from paying federal income taxes.

Less common forms of corporations include **B Corps**, which focus on a triple bottom line of profit, people, planet. They can register as either C Corps or S Corps but must show they are committed to social and environmental sustainability, public transparency and legal accountability. Close corporations are more like partnerships but allow for some corporate benefits with certain limitations. Shareholders are capped between 30 and 35, depending on the state, and stocks cannot be made public. Close corporations must register with the state in which they are incorporated, and not all states recognize them. They are more expensive to create because they also must have a written shareholder agreement to outline the relationship between the corporation and its shareholders.

This resource is part of American Farmland Trust's Farm Transfer Toolkit which is available on AFT's Farmland Information Center website. The toolkit walks agricultural landowners through key steps in a farm transfer process. It contains information, worksheets and other tools to help users set goals, assess their finances, communicate with stakeholders, and work with professionals to finalize decisions and implement a transfer plan.