

Labor can be valued by using a typical wage rate for performing comparable work. A reasonable estimate for management is more difficult to estimate, but a rule of thumb frequently used is to take ten percent of all other costs.

Net income (net of direct expenses) is then shared in the same proportion as each party's respective contribution of resources.

Example

In the example below, the annual value (cost) of the first party's contribution is \$69,000, or 60 percent of the total. The second party contributes \$46,000, or 40 percent of the total.

Table 1. Annual value of contributions.

	First party	Second party	Total
Real Estate	\$35,000	\$15,000	\$50,000
Equipment	16,000	7,000	23,000
Working capital	1,000	1,000	2,000
Labor	12,000	18,000	30,000
Management	5,000	5,000	10,000
Total	\$69,000	\$46,000	\$115,000
Income party's net income share	$\frac{69,000}{115,000}$	= 60%	
Second party's net income share	$\frac{46,000}{115,000}$	= 40%	

As shown below, the gross return from the year's activities is \$166,000 with \$46,000 of direct expenses. Of the \$120,000 of net returns, the first party receives a net return of \$72,000 and the second party receives \$48,000.

Table 2. Net return.

	First party	Second party	Total
Gross income			\$166,000
Direct expenses			<u>-46,000</u>
Total net return			\$120,000
Percent distribution	60%	40%	
Individual net return	\$72,000	\$48,000	\$120,000

50/50 Model

In the 50/50 model, the contributions of real estate, machinery and equipment, working capital, labor and management are paid a return similar to a rental payment or a wage. The amounts can be computed in the same way as they are with the Contributions Model. The remaining return (profit) is shared equally among the parties.

Example

In the following example, net business income of \$120,000 is computed by subtracting the direct business expenses from the gross income. Next a return equal to a rental fee or cost of ownership is paid to each party for the use of land, machinery, labor and management. The remaining \$5,000 of profit is divided equally between the two parties.

Table 3. Income and expenses.

Income and expenses	Total
Gross income	\$166,000
Direct expenses	<u>- 46,000</u>
Net return	\$120,000
First party's real estate	\$-35,000
Second party's real estate	- 15,000
First party's equipment	- 16,000
Second party's equipment	- 7,000
First party's working capital	-1,000
Second party's working capital	-1,000
First party's labor & management	- 17,000
Second party's labor & management	<u>- 23,000</u>
Profit	\$5,000

Each party's total return consists of the rental or wage return from his/her respective resources plus 50% of the profits. As shown below, the first party receives \$71,500 and the second party \$48,500.

	First party	Second party	Total
Real Estate	\$35,000	\$15,000	\$50,000
Machinery & equip.	16,000	7,000	23,000
Working capital	1,000	1,000	2,000
Labor & mgmt.	17,000	23,000	40,000
Profit	2,500	2,500	5,000
Net return	\$71,500	\$48,500	\$120,000

A Decision Tool for Dividing Business Income is available at: <http://www.extension.iastate.edu/agdm/wholefarm/xls/c1-51dividingincome.xls>.