

SHARING FARM MACHINERY OWNERSHIP ALTERNATIVES

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Why Share Machinery?

- Manage operating costs
 - Costs of owning and operating farm machinery make up about 20-30 percent of annual per acre cost of raising corn and soybeans
 - Some estimates peg it as high as 40 percent
- More fully utilize the machine

Ways to Structure Shared Machinery Arrangements

- Sole ownership with a custom agreement
 - One person owns the machine and is responsible for ownership costs
 - Machine owner signs a custom agreement with another farmer for a set fee
 - Parties may share labor (or may not)

Ways to Structure Shared Machinery Arrangements

⦿ Joint purchase (Partnership)

- Each party responsible for proportionate part of interest and principal payments
- Must establish bank account
 - Each party contributes agreed amount per acre to pay for repairs, insurance and storage, etc.
 - Party with more acres typically pays custom rates on excess acres

Partnership Arrangements

- What if a partner dies?
 - Surviving owner usually given first option to buy machinery at appraised price or at a price based on a previously agreed-upon depreciation schedule
 - If option not exercised, machine sold at auction and proceeds split between estate of deceased partner and survivor

Partnership Arrangements

- ⦿ Should be reduced to writing
 - Death
 - Divorce
 - Dissolution

Joint-Ownership

● Tenants-in-Common

- Undivided interest that passes to a deceased tenant's heirs upon death
 - For more expensive items, may want to consider “cross” life insurance on each other owner for purposes of buying out the deceased owner's heirs

Joint Ownership

- ① Joint tenancy

- Works well in parent-child situations
 - Surviving co-owner gets machine upon death of other co-owner

Joint Ownership or Partnership

- Care must be taken to distinguish the types of organization
 - Rights to assets upon death of a “partner”

Machinery Cooperatives

⦿ Advantages

- Helps control the “timeliness” issue
- Reduction in capital invested by individual farmers in machinery
- Economies of scale
- Savings in operating costs
- Enable smaller farms to take advantage of technological changes with lower financial commitments
- Price discounts (due to volume)

Machinery Cooperatives

⦿ Limitations

- Timeliness – more than one member may want to use a piece of equipment during the same time
 - Establish a harvesting schedule
- Must maintain good working relationships among members

Machinery Cooperatives

- ⦿ Democratic control – “one-member, one-vote”
- ⦿ Co-op is incorporated – limits members’ liability to amount invested

Machinery Cooperatives

⦿ Types

- Piece-by-piece machinery sharing
- Sharing of complete farm machinery sets
- Pooled production
- Non-pooled production
- Labor sharing

Other Points on Machinery Ownership Structures

- Individuals, corporations, LLCs, and LPs may be “persons” for payment limitation purposes
 - But, corporations in which more than 50 percent of the interest is owned by the individual’s spouse, and minor children or by an entity is not a separate person

Payment Limitation Issues

- GPs and joint ventures (known as joint operations), as well as cooperative marketing associations are not eligible for “person” status, but the individual members may be

Payment Limitation Issues

- GPs and joint ventures tend to be more advantageous for payment limitation purposes than corporations, LLCs and limited partnerships
 - Liability concerns can be limited by forming a partnership of single-member LLCs

Why Does the Type of Sharing Arrangement Matter?

● Liability issues

- No protection in sole proprietorship
 - Need to ensure that custom operator is an independent contractor
- Partnership
 - Joint and several liability
- Limited Liability Partnership
 - Protection for limited partners in LLP

Limited Liability Company

- ⦿ Lower cost, simpler alternative to the corporation
- ⦿ Typically lower state formation and renewal fees
- ⦿ Less complex and burdensome operating rules
- ⦿ Better asset protection for the owner's business against the claims of personal creditors
- ⦿ Better integration with other estate planning techniques

LLCs and Taxation

- Treated as a sole proprietorship if one owner
- Generally treated as general partnership if multiple owners unless election made to treat as partnership

What is Better – LLC or LLP?

- Owners of LLP have only a reduced form of liability from the claims of the business's creditors (limited shield)
- Typically works well for a large business that is operating as a general partnership

What is Better – LLC or LLP?

- LLC assets are not shielded from liability with respect to business debts
- Charging order concept:
 - If partner incurs large personal debt from non-business activities which cannot be satisfied from partner's personal assets, personal creditor can get a charging order against partner's interest in the partnership – can attach the partnership interest but not underlying assets.

Liability – In General

- Common sense
 - Proper use of equipment
 - Safety guards in place and operational
 - Training
 - Insurance
 - Proper use of chemicals
 - Relationships with neighbors
 - Dust, lights, pollen drift, etc.