



PennState Law

Center for Agricultural
and Shale Law





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Legal Planning for Specialty Crop Producers: Understanding Liability Protections, Regulatory Processes, and Other Legal Risks



A multi-part 2022 educational series to assist Pennsylvania specialty crop producers successfully augment wholesale sales revenue with income from direct sales, pick-your-own, value-added commodity processing, or agritourism, agritainment & educational activities, Penn State Law's Center for Agricultural and Shale Law is conducting an educational series of workshops and webinars over the coming year about the prevention and planning necessary to best avoid contractual, tort, and regulatory liabilities in conducting income-augmenting activities.

Visit our website at aglaw.psu.edu for registration and details.

Topic #1

Legal Liability Risks from Business Invitees on the Farm

This topic will examine the ways in which legal liability can arise from the care, custody, and control of real estate upon which visitors are invited for the purpose of doing business with a specialty crop producer, as well as liability insurance coverage, waivers, etc.

- Wednesday, Mar. 9, 2022, 12 noon, via Zoom. Register at aglaw.psu.edu

Topic #2

Legal Liabilities in Selling Raw and Processed Specialty Crop Products

This topic will educate producers on the various theories of contractual, warranty, and common law legal liabilities, including “products liability,” that can arise from the production and sale of both raw agricultural products and value-added processed products, as well as how insurance may protect against such claims.

- Wednesday, Mar. 23, 2022, 12 noon, via Zoom. Register at aglaw.psu.edu

Topic # 3

Business Structures for Operational Resilience and Liability Avoidance

This topic will review the various forms of business entity structures that may be employed by specialty crop producers, the attributes and pros and cons of each, the formalities that must be followed to maintain financial and legal liability protections.

- Wednesday, Apr. 6, 2022, 12 noon, via Zoom. Register at aglaw.psu.edu



Spring 2022 Sessions



Topic #4

Licensing and Regulatory Obligations in Selling Raw and Processed Specialty Crop Products

This topic will educate producers on the state laws and county/municipal ordinances that regulate the activity of producing and selling foods for human consumption, including health/food code licensing requirements for the storage, production and sale of food, sales tax licensing and collection, and other regulatory requirements that may apply in particular contexts, venues, or jurisdictions.

- Wednesday Nov. 16, 2022, 12 noon, via Zoom. Register at aglaw.psu.edu

Topic #5

Municipal Law & Zoning for Agritourism / Agritainment, Specialty Crop Processing & Sales

This topic will provide producers an understanding of local municipal government requirements and procedure for permits and approvals that may be required for agritourism, agritainment, processing, and sales activities conducted in conjunction with the production of specialty crops.

- Wednesday, Nov. 30, 2022, 12 noon, via Zoom. Register at aglaw.psu.edu

Topic #6

Statutory Protections/Restrictions: Understanding PA's Ag Area Security, Right-To-Farm, ACRE, and Clean & Green Laws for Specialty Crop Producers

This topic will instruct producers on how to understand the scope of, and potentially employ, the various statutory protections in Pennsylvania law for agricultural operations, and frequently also available in other jurisdictions. It will also examine business operation limitations that arise from voluntary enrollment in governmental benefit programs which seek to preserve agricultural uses of land.

- Wednesday, Dec. 14, 2022, 12 noon, via Zoom. Register at aglaw.psu.edu



Fall 2022 Sessions





Thanks to our Partners

This presentation was created as part of the
Pennsylvania Specialty Crop Block Grant Program



**Agricultural
Marketing
Service**



pennsylvania
DEPARTMENT OF AGRICULTURE

Specialty Crop Block Grant Program



Topic #3

Business Structures for Operational Resilience and Liability Avoidance



April 6, 2022



Topic #3

**Business Structures for Operational
Resilience and Liability Avoidance**



Objective

This topic will review the various forms of business entity structures that may be employed by specialty crop producers, the attributes and pros and cons of each, the formality that must be followed to maintain financial and legal liability protections.



Overview

- Why choose a business structure?
- The various factors to consider.
- Basics of the 6 most common business entities.
 - characteristics, formation, operation, taxation.



SEEK YOUR OWN LEGAL COUNSEL FOR YOUR OWN SITUATION.

(THIS SESSION IS PREPARATION FOR MAKING THE BEST USE OF YOUR ATTORNEY'S TIME.)



7 FACTORS TO CONSIDER

1. Liability
2. Taxes
3. Ownership and Management
4. Authority and Formalities
5. Capitalization
6. Transfer and Estate Planning
7. Government Program payments



1. FACTOR TO CONSIDER - LIABILITY

- Protection from personal liability.
- Liability may be financial or personal injury/property damage.
- Not a replacement for insurance.



2. FACTOR TO CONSIDER - TAXES

- Entity level taxation.
- Pass-through taxation.
- Tax law changes - can happen quickly.
 - That's why you consult an accountant and/or attorney.



3. FACTOR TO CONSIDER - OWNERSHIP

- Flexibility vs rigidity.
- For example:
 - Limited partner vs. general partner.
 - Non-voting shareholder vs. voting shareholder.
 - LLC is viewed as the ultimate in flexibility (with an appropriate Operating Agreement).



4. FACTOR TO CONSIDER - AUTHORITY

- Individual authority – who can bind?
- Ownership authority – internal decision-making req.
- Business formalities – documenting internal decisions.



5. FACTOR TO CONSIDER – CAPITALIZATION

- Adding assets to the business – incl. in-kind contrib.
- Not adding assets to the business – “this tractor is mine.”
- Incurring debt to capitalize – Do you want every business debt to be a personal debt, with all that entails?



6. FACTOR TO CONSIDER – TRANSFER AND ESTATE PLANNING

- Facilitate transfer as shares or units instead of individual assets.
- Some provide protection for retiring generation, e.g. limited partnerships.
 - Gifting or sales may be discounted in some cases.
- Unexpected death/disability can destroy a business.



7. FACTOR TO CONSIDER – GOVT PROGRAMS

- Payments can be impacted by legal entity type and structure.
- “Active engagement” matters – AEF.
- Payments can have per person and/or per entity limits, e.g. AGI.



**Your factors to consider
may be different than
other farmers' factors.
There is no single correct
business structure for
everyone.**

1. Liability
2. Taxes
3. Ownership and Management
4. Authority and Formalities
5. Capitalization
6. Transfer and Estate Planning
7. Government Program payments



Do I need a business entity?

- Businesses can be run without formal structure.
- However, the business operators' personal assets will be at risk from business debts or liabilities.
- Available tax benefits may be lost.
- Managing assets, capital investment and operations needs structure when >1 person.



6 MOST COMMON BUSINESS STRUCTURES

1. Sole Proprietorship
2. General Partnership
3. Limited Liability Company
4. Limited Partnership
5. C Corporation
6. S Corporation

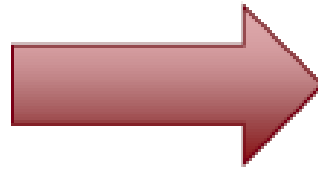


1. Sole Proprietorship

- Easy to set up and conduct/maintain.
- Not technically separate from the owner.
- Business assets and liabilities are owned by operator.
- No corporate formalities.
- Held personally responsible for business liabilities.
- Q: Is the spouse really part of a partnership, rendering assets held as a married couple liable for business debts?



Sole
Proprietor



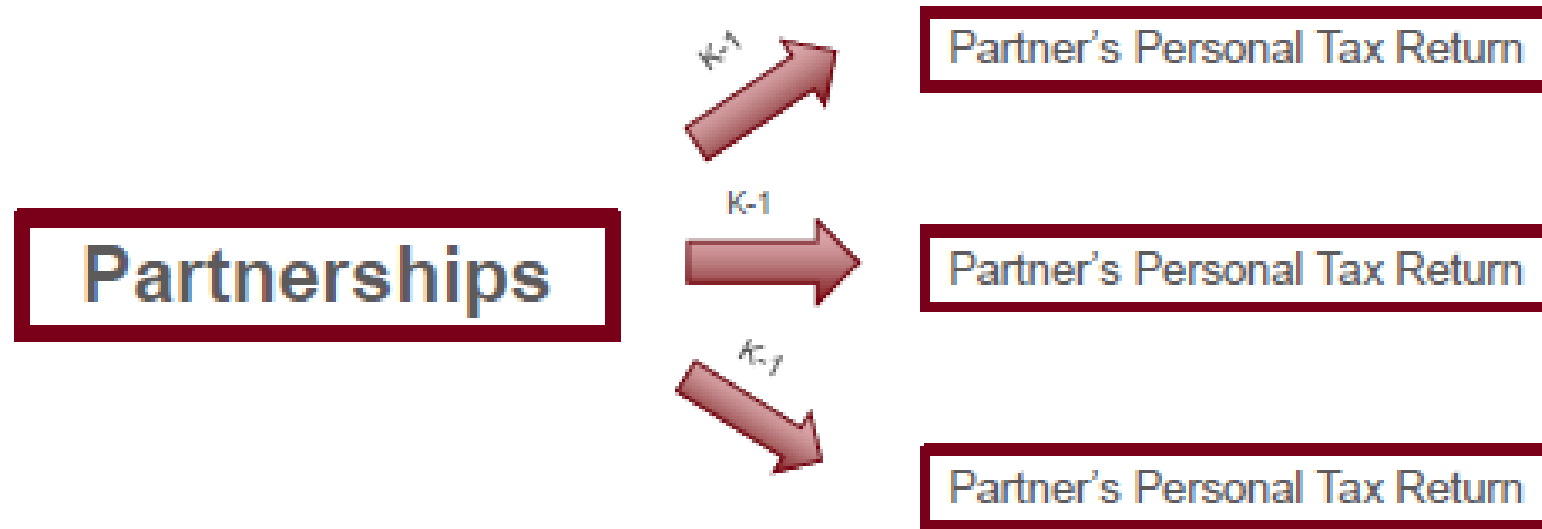
Schedule F
Or
Schedule C
on 1040

- Sole Proprietor reports business income on his/her personal tax return



2. Partnership (General Partnership – “GP”)

- Similar to sole proprietorship, but 2 or more people.
- Easy set up. Many are “informal” w/o paperwork.
- Managing workload shared with partners.
- More assets with more people.
- All partners’ personal assets are available to satisfy business liabilities.
- Potential for personal conflicts between partners.
- Optional - governed by a “Partnership Agreement.”

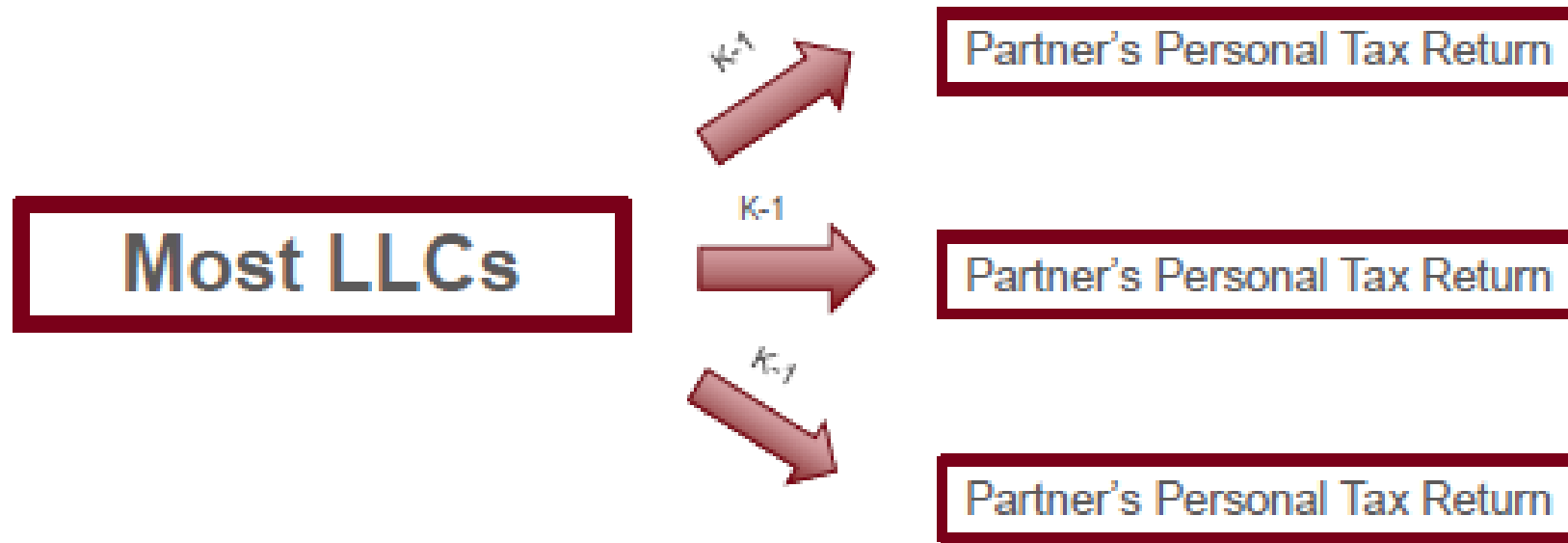


- Partner's share of profits (loss) passes from a partnership to the individuals' return(s)
- No income tax is paid at the partnership level
- All business income subject to self employment tax



3. Limited Liability Company (LLC)

- Separate legal entity, may have as few as one member.
- Owner(s) decides how to be treated for taxes.
- Most often treated as a pass-through partnership for taxation.
- Personal Assets are not available to satisfy business liabilities.
- Optional – governed by “Operating Agreement.”



- Earnings from LLC subject to Self-Employment Tax



4. Limited Partnership (LP)

- Two or more persons involved
- General partner oversees the business
- Limited partners do not partake in management of the business
- General Partner's personal assets are exposed to business liabilities whereas the Limited Partner's personal assets are not exposed to business liabilities.
- Pass through taxation.



5. C Corporation

- Pay income taxes on profits earned by the business.
- Income generated by business is distributed to shareholders as dividends or salary paid to working owners (sometimes also as rent if assets are leased to the corporation).
 - This is taxed at the individual owners' rate.
- Excess retained earnings subject to accumulated earnings tax.
- This is referred to as ***“double taxation.”***
- Potentially more deductions and lower self-employment (SE) tax.



5. C Corporation (cont.) – features

- Corporations protect personal assets from business liabilities.
- Corporation protection of personal assets requires adherence to certain practices (no co-mingled funds, corporate formalities).
- Corporations require a strict governance structure: shareholders, directors, and officers.
- Be sure the farm operation has enough money (“sufficiently capitalized”) and keep the corporation’s financial affairs separate from the shareholders’ financial affairs.

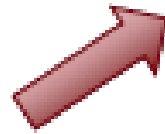


5. C Corporation (cont.) – formalities

- Appoint the initial directors, the deciders of big decisions.
- Draft and file the articles of incorporation with the state.
- Draft and adhere to corporate bylaws.
- Hold an initial organizational meeting: adopt bylaws, elect officers, approve issuance of stock, issue stock.
- Create a shareholder agreement if the shareholders want one.
- Hold annual meetings & adhere to formalities or . . . →
“Pierce the Corporate Veil” (lose protection from personal liability).



**C Corporation
pays it's own
tax and pays
wages, rent,
and
distributes
dividends**



Shareholders



Shareholders

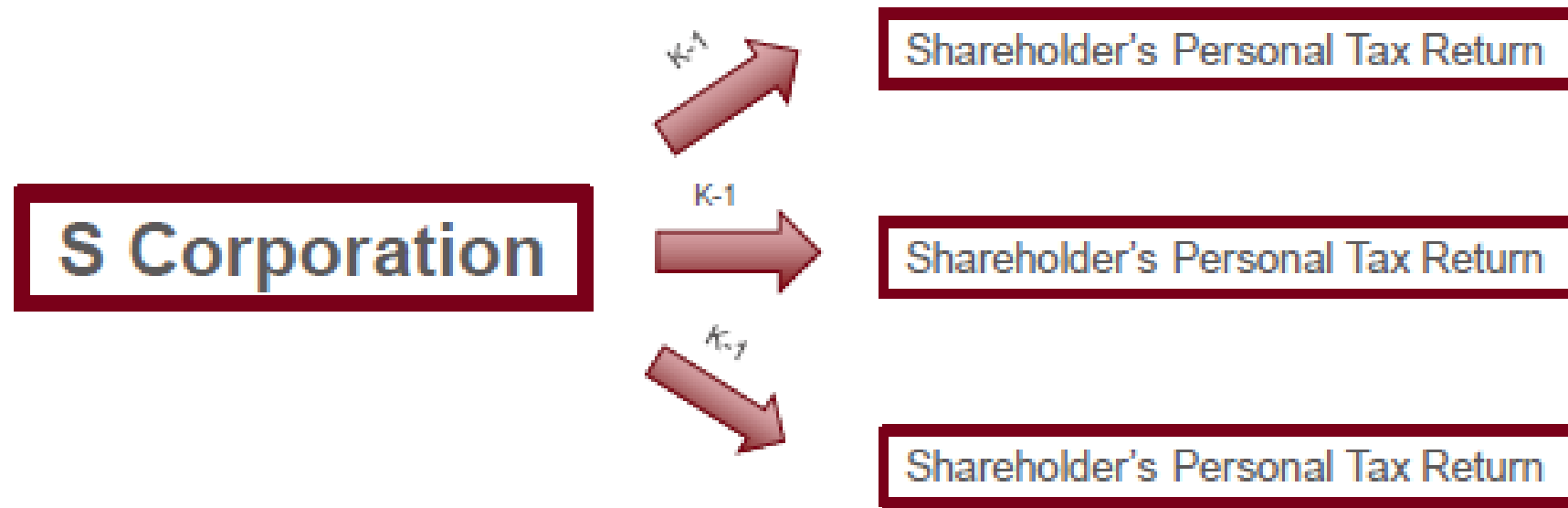


Shareholders



6. S Corporation

- File a business tax return and each owner a K-1.
- Profit or loss are “passed-through” to the owners and taxed at individual tax rates.
- Pass-through profits not subject to SE tax.
- Required to pay salary to shareholders.
- More formal rules and procedures than partnership.
- Personal asset protection from business liabilities, **IF** all the same corporate formalities as a “C” are followed.



- Earnings from LLC subject to Self-Employment Tax
- S Corp must pay shareholders a salary.



Characteristics / Entities	Tax Treatment
C Corporations	Corporation taxed on its earnings at the corporate level and the shareholders have a further tax on any dividends distributed (double taxation)
S Corporations	Entity generally not taxed as the profits and losses are passed through to the shareholders (pass through taxation)
Sole Proprietorship	Entity not taxed, as the profits and losses are passed through to the sole proprietor
General Partnership	Entity not taxed as the profits and losses are passed through to the general partners
Limited Partnership (LP)	Entity not taxed as the profits and losses are passed through to the general and limited partners
Limited Liability Company (LLC)	Entity not taxed (unless chosen to be taxed) as the profits and losses are passed through to the members



1. Sole Proprietorship
2. General Partnership
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PA Formation Filing Requirements

- Pennsylvania Department of State, Corporation Bureau
 - ✓ Required: Articles of Incorporation for S and C Corp.
 - ✓ Required: Certificate of Organization for LLC.
 - ✓ Required: Certificate of Limited Partnership for LP.
- Optional – Registration of Fictitious Name for any entity.
 - Required to protect name, except S, C, LLC, or LP.
- Optional – Certificate of Partnership Authority for GP.



Thank you! Q & A?

Brook Duer

Staff Attorney

Center for Agricultural and Shale Law

Penn State Law

329 Innovation Boulevard, Suite 118

University Park, PA 16802

(814) 863-3396

dhd5103@psu.edu





**PENN STATE CENTER FOR
AGRICULTURAL AND SHALE LAW**

329 Innovation Blvd., Suite 118
University Park, PA 16802
Phone: 814-865-4290
Fax: 814-865-3851
Website: AgLaw.psu.edu

PROFESSIONAL STAFF

Center Director

Ross H. Pifer
rpifer@psu.edu

Staff Attorney

Brook Duer
dhd5103@psu.edu

Staff Attorney

Jackie Schweichler
jks251@psu.edu

Research Specialist

Chloe Marie, LL.M.
cjm445@psu.edu

CENTER MISSION AND BACKGROUND

The Center for Agricultural and Shale Law conducts research and educational programs to serve a wide variety of stakeholders including agricultural producers, landowners, mineral interest and royalty owners, business professionals, judges, attorneys, legislators, government officials, community groups, and the general public. Center programs are funded in part by the Commonwealth of Pennsylvania through the Pennsylvania Department of Agriculture. The Center for Agricultural and Shale Law is a partner of the National Agricultural Law Center (NALC) at the University of Arkansas System Division of Agriculture, which serves as the nation's leading source of agricultural and food law research and information.

This publication is available in alternative media upon request. Penn State is committed to affirmative action, equal opportunity, and the diversity of its workforce.





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April 6, 2022