



PennState Law

Center for Agricultural
and Shale Law

Legal (and Tax) Structures for Business and Land Ownership

11:15 am – 12 noon

12:45 pm – 1:30 pm

Beginning Farmer Intensive: Land, Law and Transition



USDA National Institute of Food and Agriculture

U.S. DEPARTMENT OF AGRICULTURE

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- 18 years in private practice in Lancaster County
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- Penn State Ag Law Center since 2019.



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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.

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Welcome to the Center for Agricultural and Shale Law

- **Agricultural Law Weekly Review**
- **Agricultural Law Virtual Resource Rooms**
- **Agricultural Law Trackers**
- **Agricultural Law Podcast**
- **Videos/Presentations**
- **PA Ag Mediation Program**

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Agricultural Law Virtual Resource Rooms



ACRE/Pennsylvania Act 38



Pennsylvania Agricultural Area Security Law



Pennsylvania Right to Farm Act



Pennsylvania Clean and Green Act



Pesticide & Herbicide Non-Target Injury



Solar Electricity Generation on Rural Lands



HOME › ISSUE TRACKERS › AGRICULTURAL LAW ISSUE TRACKERS

Agricultural Law Issue Trackers



[Ag Gag Statutes](#)



[Agricultural Antitrust Litigation](#)



[Animal Confinement](#)



[Dicamba](#)



[Genetically Modified Salmon](#)



[Glyphosate](#)

Pennsylvania Agricultural Mediation Program



- Who can request mediation?
 - USDA-related issues:
 - Agricultural Loans
 - Wetlands determinations
 - Compliance with farm programs, including conservation programs
 - National organic program established under the Organic Foods Production Act of 1990
 - Agricultural Credit
 - Rural water loan programs
 - Grazing on National Forest System land
 - Pesticides
 - Non-USDA issues:
 - Land and Equipment Lease issues.
 - Family farm transition.
 - Farmer-neighbor disputes.
 - As approved by PA Secretary of Agriculture

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Introduction To Business Structures

- Partnerships, Corporations, Limited Liability Companies (LLC), etc.
- How they operate; Pros and Cons; How they help manage liability & facilitate growth; Transfer of ownership interests (*as a going concern vs. dismantling or transferring assets piecemeal*).





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. Transfers 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 (“actively engaged in farming” requirements).
- Payments can have per person and/or per entity limits, e.g. AGI (“adjusted gross income” thresholds).



***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.



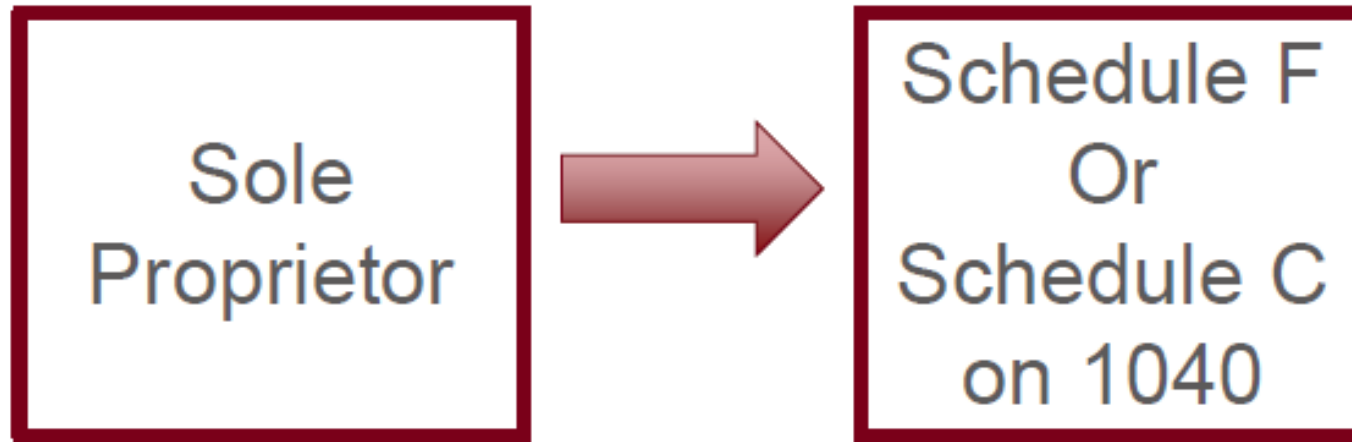
6 MOST COMMON BUSINESS STRUCTURES

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 a spouse part of a H/W or ***spousal partnership***, rendering assets held as a married couple liable for business debts?

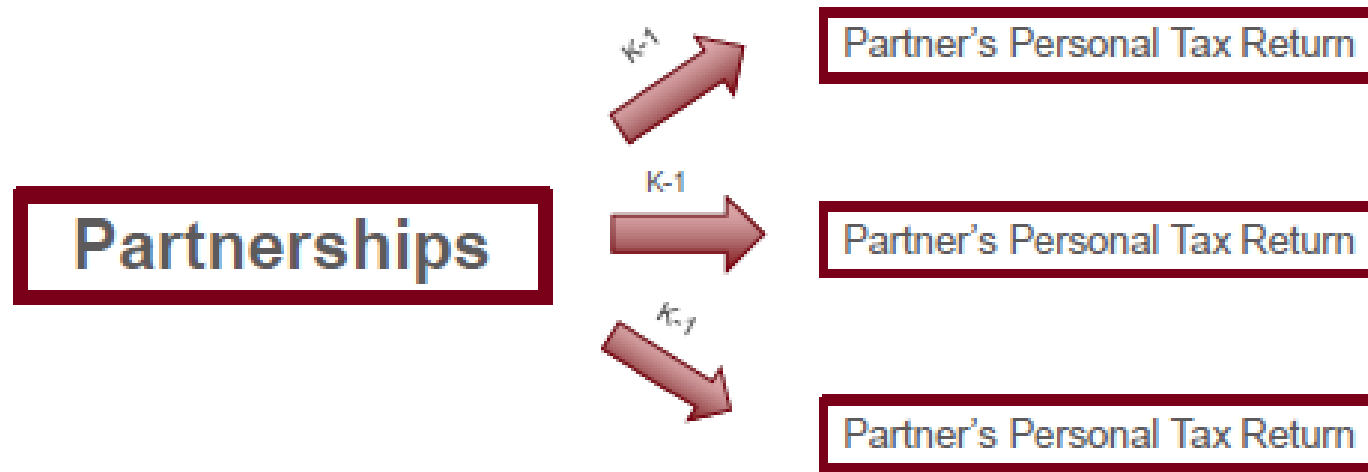


- Sole Proprietor reports business income on his/her personal tax return



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 disruptive personal conflicts between partners.
- Optional - govern by a “Partnership Agreement.”

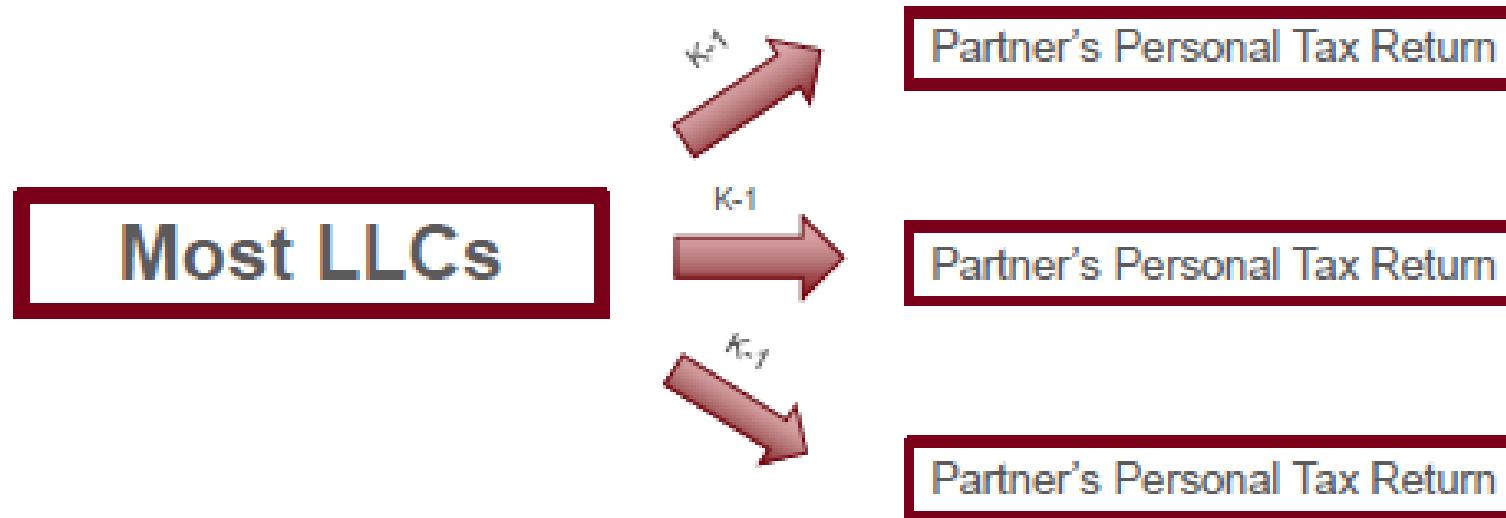


- Partner's share of profits (loss) passes from a partnership to the individuals' return(s)
- No income tax is paid at the partnership level
- All business income subject to self employment tax



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: **pass-through taxation** – *members pay income tax individually.*
- 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 just like any partnership.



5. C Corporation

- Corp. pays income tax on profits earned by the business.
- Income generally distributed to shareholders as dividends or salary to working owners (sometimes also as rent if assets are leased to the corporation).
 - This is taxed at the individual owners' rate in tax return.
- This scenario is referred to as ***“double taxation.”***
- Corporate income tax paid plus excess retained earnings are potentially subject to accumulated earnings tax.
- Potentially more deductions and lower self-employment (SS and Medicare) taxes.



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.



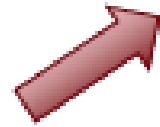
5. C Corporation (cont.) – formalities

- Governed by a board of directors and corporate officeholders.
- 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).



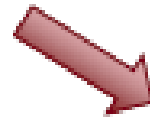
**C Corporation
pays it's own
tax and pays
wages, rent,
and
distributes
dividends**



Shareholders



Shareholders

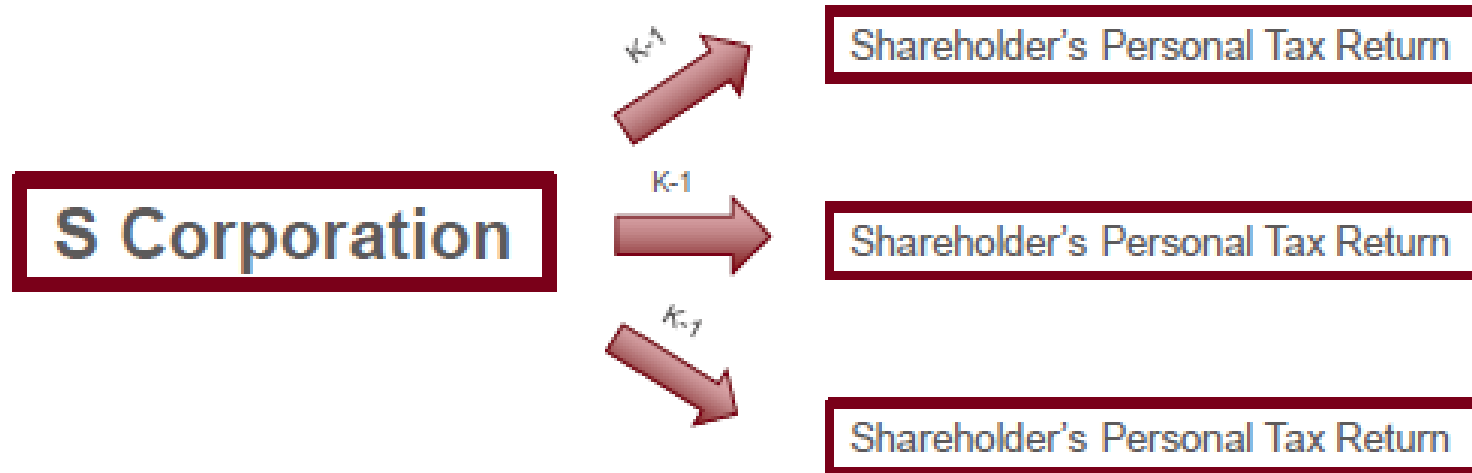


Shareholders



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 self-employment tax at corp. level.
- Required to pay salary to shareholders.
- More formal rules and procedures than a partnership.
- Personal asset protection from business liabilities, **IF** all the same corporate formalities of 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



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 best protect name, except S, C, LLC, or LP.
- Optional – Certificate of Partnership Authority for a General Partnership.

1. Sole Proprietorship
2. General Partnership
3. Limited Liability Company
4. Limited Partnership
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While you are at it, don't forget the basic tools of Estate (*and Business!*) Planning

- Will
- Durable Power of Attorney
- Healthcare Power of Attorney
- Advance Medical Directive (“Living Will”)



Land Ownership Structures

Accomplished by Deed in the following common forms:

- Sole Ownership
- Joint Tenants
- Tenants in Common
- Tenants by the Entirety (marriage)
- Corporate
- Partnership
- Trust



Joint Tenants (JT)

- 2 or more persons or entities hold title.
- Equal ownership rights to entire property – “undivided interests.”
- Not “freely alienable” – transfer would dissolve the joint tenancy.
- “Right of Survivorship” - Upon death, joint interest automatically passes to the remaining surviving joint tenants by operation of deed, avoids probate.
- The “undivided interests” are potentially subject to each owner’s individual debts/creditors. Creditor of one is creditor of all.
- ***Partition action*** to dissolve the joint tenancy must be filed by a creditor to satisfy debt.



Tenants in Common (Co-Tenancy) (TIC)

- Two or more persons or entities hold title.
- Undivided interests. (% ownership can be specified)
- No rights of survivorship. The co-tenancy interest subject to probate.
- Freely “alienable” interests. Each co-tenant can sell or encumber their share apart from the others.
- Entire property not subject to all individual co-tenant’s debts – creditor of one is NOT a creditor of all. Creditors can only reach the co-tenant’s share.
- Partition action can be filed by creditor, does not dissolve the co-tenancy.



Tenants by the Entirety (T/E)

- For two married persons only.
- The couple is “one person” for legal purposes.
- Automatically passes to the surviving spouse upon death, avoids probate.
- Not subject to debts of an individual spouse (incurred before or after date of marriage).
- Upon divorce, automatic conversion to tenants in common.
- This is the most fundamental liability protection in operating a business.
Ex: Farm operated by an LLC, husband and wife are members of the LLC and lease the acreage to the LLC. LLC pays rent, or not (depends upon tax and other implications).



Sole Ownership

- Certainly, it can be done and is done.
- If an individual person, it creates a whole host of problems upon death if the land is being used for a farming operation which is anticipated to continue after that person's death.



P-ship, Corporate & Trusts

- A deed in the name of a partnership is just a form of JT, TIC or T/E (if married). *Also: Limited Partnerships (one general partner, and an unlimited amount of limited partners).*
- Corporate land ownership is generally inadvisable due to double taxation.
- Trusts – the permutations are nearly endless.
 - The overriding purpose is to create an entity wholly independent but with its own “marching orders” administered by a trustee(s) for whatever specific purposes and beneficiaries are articulated in the trust documents.



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Thank you for your attention.

QUESTIONS?

