



**Four Basic Types** p. 1

- Sole Proprietorship
- Partnership
- Corporation
- Limited Liability Company

**Sole Proprietorships** p. 1

- One owner who has full control
- Liable for all debts of the business
- No formalities are required to form a sole proprietorship
- Owner pays tax on all business income

**Partnerships** p. 1

A partnership is an association of two or more persons sharing the profits and losses from a business.

**Partnerships** pp. 1-2

- General partnership
  - All partners are liable for partnership debt
- Limited partnership
  - At least one general partner
  - At least one limited partner

**Income Taxation of Partnerships** p. 2

- Partnership does not pay taxes
- Partners report their shares of income or loss
- Gain or loss is not recognized when assets are transferred into or out of a partnership

### Example 1

p. 2

FMV of land	\$600,000
Partner's basis	<u>50,000</u>
Realized gain	\$550,000
Recognized gain	0
Partnership's basis	\$ 50,000

### Corporations

p. 2

- Limited liability
- More formalities than a partnership
  - Shareholders
  - Directors
  - Officers

### Income Taxation of Corporations

p. 4

- Corporation pays taxes on its income
- Dividends are taxable income to shareholders
- When assets are distributed, gains are taxed at both corporate and shareholder level
- Shareholders can be employees

### Example 2

p. 4

FMV of land	\$600,000
Shareholder's basis	<u>50,000</u>
Realized gain	\$550,000
Recognized gain	0
Corporation's basis	\$ 50,000

### S Corporation

p. 4

- Restrictions on number and type of shareholders
- Income taxed only at shareholder level
- Gain taxed at shareholder level when assets are distributed

### Limited Liability Company

p. 5

- Taxed as a partnership
- Limited liability like a corporation

## Planning for the Farm Business Arrangement p. 6

- Decision making
- Formation
  1. Sell assets to LLC
  2. Rent assets to LLC
  3. Compensate with guaranteed payments
  4. Divide profits among members

## Example 3 p. 7

- Anne contributed 90% of assets
- Andy contributed 10% of assets
- Each contributes 50% of labor and management

## Operating LLC p. 8

- Start with equal ownership
- Start with unequal ownership and adjust over time