ASSIGNMENT

ON

BUSINESS STRUCTURES OF FARMS

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INTRODUCTION

Agribusiness include not only that productive piece of land but also the people and firms that provide the inputs (i.e. Seed, chemicals, credit etc.), process the output (i.e. Milk, grain, meat etc.), manufacture the food products (i.e. ice cream, bread, breakfast cereals etc.), and transport and sell the food products to consumers (i.e. restaurants, supermarkets etc.). Farmers found it increasingly profitable to concentrate on production and began to purchase inputs they formerly made themselves. This trend enabled others to build business that focused on meeting the need for inputs used in production agriculture such as seed, fencing, machinery and so on. These farms involved into the industries that make up the “agricultural inputs sector”. Input farms are major part of agribusiness and produce variety of technologically based products that account for approximately 75 per cent of all the inputs used in production agriculture.

At the same time the agriculture input sector was evolving, a similar evaluation was taking place a commodity processing and food manufacturing moved off the farm. The form of most commodities (wheat, rice, milk, livestock and so on) must be changed to make them more useful and convenient for consumers. For ex. consumers would rather buy flour than grind the wheat themselves before backing a cake. They are willing to pay extra for the convenience of buying the processed commodity (flour) instead of the raw agriculture commodity (wheat). During the same period technological advance were being made in food preservation method. Up until this time the perishable nature of most agriculture commodities meant that they were available only at harvest. Advance in food processing have made it possible to get those commodities all throughout the year. Today even most farm families use purchased food and fiber products rather than doing the processing themselves. The farms that meet the consumers demand for greater processing and
convenience also constitute a major part of agribusiness and are referred to as the processing manufacturing sector.

**FEATURES AND SCOPE OF AGRIBUSINESS**

It is apparent that the definition of agriculture had to be expanded to include more than production. Farmers rely on the input industries to provide the products and service they need to produce agricultural commodities. They also rely on commodity processors, food manufactures, and ultimately food distributors and retailers to purchase their raw agricultural commodities and to process and deliver them to the consumer for final sale. The result is the food and fiber system.

The food and fiber system is increasingly being referred to as “agribusiness”. The term agribusiness was first introduced by Davis and Goldberg in 1957. Agribusiness represents three part system made up of;

(1) The agricultural input sector

(2) The production sector

(3) The processing-manufacturing sector

The capture the full meaning of the term “agribusiness” it is important to visualizes these three sectors as interrelated parts of a system in which the success of each part depends heavily on the proper functioning of the other two. It was already indicated that agribusiness is a complex, system of input sector, production sector, processing manufacturing sector and transport and marketing sector. Therefore, it is directly related to industry, commence and trade, Industry is concerned with the production of commodities and materials while commerce and trade are concerned with their distribution.
Today the business has become very competitive and complex. This is mainly due to changing taste and fashion of the consumers on the one hand, and introduction of substitute and cheaper and better competitive goods, on the other. The old dictum “produce and sells has changed overtime into “produce only what customers want”.

FARM BUSINESS STRUCTURES

Business structures are established with the objective of making profits. They can be established either by one person or by a group of persons in the private sector by the government or other public bodies in the public sector. A business started by only one person is called sole proprietorship. The business started by a group of persons can be either a Joint Hindu Family or Partnership or Joint Stock Company or a Co-operative form of organization. Thus there are three legal forms of agribusiness organization:

- Sole Proprietorship
- Partnership Firm
- Joint Stock Company or Corporation

Structures of business organization are legal structures in which a business enterprise may be organized and operated. These structures of organization refer to such aspects as ownership, risk bearing, control and distribution of profit. Any one of the above mentioned structures may be adopted for establishing a business, but usually one form is more suitable than other for a particular enterprise. The choice will depend on various factors like the nature of business, the objective, the capital required, the scale of operations, state control, legal requirements and so on. Out of the forms of private ownership listed above the first three forms (1, 2, and 3) may
be described as non-corporate and the remaining (4 and 5) as corporate forms of ownership. The basic difference between these two categories is that a non-corporate form of business can be started without registration while a corporate form of business cannot be set up without registration under the laws governing their functioning.

**Characteristics of an ideal form of organization**

- **Ease of formation:** It should be easy to form the organization. The formation should not involve many legal formalities and it should not be time consuming.

- **Adequacy of Capital:** The form of organization should facilitate the raising of the required amount of capital at a reasonable cost. If the enterprise requires a large amount of capital, the preconditions for attracting capital from the public are
  - Safety of investment
  - Fair return on investment and
  - Transferability of the holding.

- **Limit of Liability:** A business enterprise may be organized on the basis of either limited or unlimited liability. From the point of view of risk, limited liability is preferable. It means that the liability of the owner as regards the debts of the business is limited only to the amount of capital agreed to be contributed by him Unlimited liability means that even the owners’ personal assets will be liable to be attached for the payment of the business debts.
- **Direct relationship between Ownership, Control and Management:** The responsibility for management must be in the hands of the owners of the firm. If the owners have no control on the management, the firm may not be managed efficiently.

- **Continuity and Stability:** Stability is essential for any business concern. Uninterrupted existence enables the entrepreneur to formulate long-term plans for the development of the business concern.

- **Flexibility of Operations:** Another ideal characteristic of a good form of organization is flexibility of operations. Changes may take place either in market conditions or the states’ policy toward industry or in the conditions of supply of various factors of production. The nature of organization should be such as to be able to adjust itself to the changes without much difficulty.

**SOLE PROPRIETORSHIP**

A sole proprietorship or one man’s business is a form of business organization owned and managed by a single person. He is entitled to receive all the profits and bear all risk of ownership.

**The important features of sole proprietorship are:**

1. The business is owned and controlled by only one person.

2. The risk is borne by a single person and hence he derives the total benefit.

3. The liability of the owner of the business is unlimited. It means that his personal assets are also liable to be attached for the payment of the liabilities of the business.
4. The business firm has no separate legal entity apart from that of the proprietor, and so the business lacks perpetuity.

5. To set up sole proprietorship, no legal formalities are necessary, but there may be legal restrictions on the setting up of particular type of business.

6. The proprietor has complete freedom of action and he himself takes decisions relating to his firm.

7. The proprietor may take the help of members of his Family in running the business.

Advantages

1. **Ease of formation**: As no legal formalities are required to be observed.

2. **Motivation**: As all profits belong to the owner, he will take personal interest in the business.

3. **Freedom of Action**: There is none to interfere with his authority. This freedom promotes initiative and self-reliance.

4. **Quick Decision**: No need for consultation or discussion with anybody.

5. **Flexibility**: Can adapt to changing needs with comparative ease.

6. **Personal Touch**: comes into close contact with customers as he himself manages the business. This helps him to earn goodwill.

7. **Business Secrecy**: Maintaining business secrets is very important in today’s competitive world.

8. **Social Utility**: Encourages independent living and prevents concentration of economic power
Disadvantages

1. **Limited resources**: One man’s ability to gather capital will always be limited. Limited Managerial Ability.

2. **Unlimited Liability**: Will be discouraged to expand his business even when there are good prospects for earning more than what he has been doing for fear of losing his personal property.

3. **Lack of Continuity**: Uncertain future is another handicap of this type of business. If the sole proprietor dies, his business may come to an end.

4. **No Economies of Large Scale**: As the scale of operations are small, the owner cannot secure the economies and large scale buying and selling. This may raise the cost of production.

This form of business organization is most suited where:

1. The amount of capital is small

2. The nature of business is simple in character requiring quick decisions to be taken

3. Direct contact with the customer is essential and

4. The size of demand is not very large.

This form of organization also suits those individuals who have a strong drive for independent thinking and highly venturous some in their attitude.
PARTNERSHIP

A partnership is when two or more people own a business together. Each partner contributes money, property, or skills to the business and shares in the profits and losses of the business. Partnerships do not require filing articles of incorporation or formation with the Secretary of State. Initial setup is relatively simple and similar to sole proprietorships.

Taxes: Partnerships have their own Employers Identification Number (EIN), but they are not considered taxable entities. Partnerships are “pass-through” entities, meaning partners pay taxes on their share of the partnership’s profit and loss on their individual returns. A partner is taxed on his or her share of partnership profit regardless of whether the money comes to the partner. If a partnership decides to leave profit in the partnership, partners are still liable for the taxes on their share of the profit.

Liability: Partners are personally liable for all business debts, lawsuits, and judgments. Each partner is liable for all of the partnership’s obligations. If one partner defrauds a customer or lender, all of the partners are responsible for the consequences.

Decision-making/Ownership: Partners may be active or silent. Participating as a silent partner allows friends and family members who don’t want to take an active role in farm management to invest. Family members interested in transitioning farm property assets or land to future generations may consider forming family partnerships to aid in estate planning. In all cases, strong written partnership agreements are essential. Partnership agreements include the name and purpose of the business and the clearly defined expectations, contributions, and decision-making capabilities and responsibilities of each partner. Specific percentages of
profit sharing and decision-making power should also be determined in the partnership agreement. Consider employing an estate planner to allow for younger family members to transition into the partnership.

Advantages

a. **Simple to create and maintain:** There are no special formalities required to form and maintain a partnership. There is more required than for a sole proprietorship, but significantly less than a corporation or LLC.

b. **Transferability:** It is easier to transfer an interest in a partnership without having to transfer specific assets as you would with a sole proprietorship.

c. **Tax treatment:** The partnership is not a separate tax paying entity. Income, deductions and credits pass through the partnership to the individual partners who report the same on their individual returns. The double taxation issue associated with corporations is avoided.

Disadvantages

a. **Unlimited personal liability:** Each partner is jointly and severally liable for all partnership debt, meaning that if the partnership fails to pay a debt, each partner may be held liable for the full payment of the debt. Each partner is personally liable for all debts of the partnership meaning that a partner's personal non-exempt assets, as well as the business assets, may be subjected to payment of the partnership debt.

b. **Management and control:** Management of the partnership is more difficult because partners must be consulted and decisions jointly made. A formal partnership agreement is recommended to eliminate some of these concerns, and to make the business run more smoothly. Potential partners should make
sure that their personalities, goals, management styles and work habits are compatible. There will also be a loss of management and control when transferring the partnership to an heir.

c. **Tax considerations:** Partners should always seek competent tax advice before creating, changing or dissolving the partnership.

**Limited Liability Company (LLC)**

An LLC is similar to a sole proprietorship and partnership in that it is a pass-through entity, with income and losses passed to members. LLCs are not taxable entities in themselves. They differ from sole proprietorships and partnerships in that they limit the liability of their members.

LLCs are established by filing Articles of Organization with the Secretary of State and paying a filing fee. Articles of Organization include the name of the organization, date of formation, whether it’s managed by managers or members, duration of existence, business purpose, physical and mailing addresses, and names and addresses of the registered agent and executors.

**Taxes:** Taxes are filed and paid similarly as to a sole proprietorship or partnership, depending on whether the LLC is owned by an individual or two or more members. The IRS treats multiple-member LLCs like partnerships, and members pay taxes on their share of profit or loss. A member’s share of the profit or loss is called a “distributive share.” This share is based on their ownership interest in the company. Each member’s share should be specified in an LLC Operating Agreement.

**Liability:** The LLC shields its members from personal liability for all business debts, lawsuits, and judgments. Only the assets of the LLC are at risk to claims;
therefore, only members’ investments into the company are at risk. Members can be personally liable if the business is used as an extension of the person or personal finances, making it very important to keep personal and business bookkeeping separate. For example, assets used in the business should have titles in the business name, such as vehicles, etc.

**Decision-making/Ownership:** Strong Operating Agreements are essential to the establishment and operation of LLCs. Operating Agreements govern how the business makes functional and financial decisions. The agreement is signed by the members and serves as a contract binding them to its terms. Operating Agreements help limit liability of members by clearly defining the operation and differentiating it from an unprotected partnership or sole proprietorship. An Operating Agreement also clarifies any verbal agreements made by members and is a good reference in case misunderstandings arise in the future.

**Advantages**

a. It is as it describes limited liability.

b. It has less paper work and start up costs than corporations.

c. It runs a flexible operation and members determine how the profits are shared.

**Disadvantages**

a. It has a limited life. When a member leaves the LLC, it often must be dissolved.

b. The net income of LLC is subject to self-employment and tax toward medicare and social security.
C ORPORATION

A corporation is its own entity, separate from its owners. Owners are shareholders in the corporation. There are two types of corporations: S and C Corporations. The S and C stand for the subchapters where they are located in the Internal Revenue Code. In an S Corporation, the business profits and losses pass through to the shareholders who report them on their individual tax returns. There is no entity-level tax. The C Corporation is its own entity, and must pay its own income taxes on its net income. Then, shareholders also pay tax on dividends.

With all types of corporations, more attention is required in the setup and ongoing operation than with other business structures. Formation steps include choosing a corporate name, naming directors, enacting bylaws, holding meetings of board of directors, issuing stock, filing articles of incorporation with the Secretary of State, and paying a filing fee. Ongoing management of a corporation requires shareholder and director meetings and maintaining written minutes and records of major decisions or transactions.

Articles of incorporation require the name of the corporation, number of authorized shares, effective date of incorporation, expected duration of existence, and names and addresses of the registered agent and incorporators (people who formed the corporation).

**Taxes:** S Corporations follow similar reporting requirements as partnerships. The C Corporation is the only type of business that must pay its own income taxes on profits. The profits do not “pass through” as they do with other business structures. Net income is taxable to the corporation, whether that income is kept in the company or distributed to shareholders as dividends. This can result in double taxation: the profit is taxed in the corporation, and dividends are taxed as personal
income by shareholders. Corporations can avoid this with planning and advice from tax professionals. There are options to reduce double taxation, such as hiring shareholders as employees of the corporation or retaining earnings in the corporation.

One disadvantage to C Corporations is that corporate losses may not be passed through to shareholders. Another disadvantage is that if an owner transferred land into the corporation and later wants to get the land out of the corporation, the gain on the land will be taxed twice: first to the corporation and then to the shareholder. Tax on the profit from sales of assets (capital gains tax) is usually taxed at a higher rate for corporations versus individuals.

**Liability:** A corporation shields its shareholders from personal liability for all business debts, lawsuits, and judgments. Only the assets of the corporation are at risk to claims; therefore, only owners’ investments into the company are at risk.

However, shareholders are always personally liable for anything personally guaranteed. If a shareholder personally guarantees a loan to the business, the shareholder is personally responsible for that debt. Shareholders can also be personally liable if the business is used as an extension of the person or personal finances, making it very important to keep personal and business bookkeeping separate.

**Decision-making/Ownership:** A corporation is owned by all its shareholders. It usually operates with a shareholder-elected board of directors that has decision-making authority for major transactions. All corporation operations are governed by bylaws. These bylaws define when and where shareholder and board of director meetings are held, duties of officers and directors, how and when officers and directors are replaced, how corporate books are to be audited, when and how votes
are held, how the corporation makes major transactions such as contracts and loans, and how shares will be sold or transferred and dividends distributed.

**Advantages**

a. It is a limited liability.

b. It raises funds through sale of stock.

c. Potential tax savings: only wages of shareholder as employee subject to employment tax. S Corporation distributions is usually taxed at lower rate.

**Disadvantages**

a. It involves a stricter operation structure like requiring shareholders meetings etc.

b. Double taxing of C Corporations: profit taxed and dividends taxed.

c. It involves increased paper work and book keeping.

**Cooperative**

A cooperative is a business that is owned and operated by members using its services. For example, farms may join together for marketing or processing services. Cooperatives require careful setup to ensure all members agree on goals of the cooperative and strategies to achieve those goals. This usually requires several initial meetings, surveys, and feasibility analyses to ensure every member agrees with the business plan. Bylaws and membership applications must be created carefully, outlining requirements of members and the decision-making strategy members agree upon. Cooperatives are usually formed and managed similarly to corporations: filing articles of incorporation with the Secretary of State and electing a board of directors nominated by members.
**Taxes:** A cooperative operates as a corporation, but is a “pass through” entity. Similar to partnerships, S Corporations, or LLCs, members report their share of the cooperative’s profit or loss on their individual tax returns. There are specific tax codes for cooperatives; members file income tax returns using a specific 1099 form. Refer to the IRS website or a qualified accountant for more information.

**Liability:** Usually, cooperatives are operated as corporations thereby limiting liability to the members’ investment.

**Decision-making/Ownership:** The ownership of the cooperative lies in its members. They also define how decisions are made via their bylaws. This can vary among cooperatives. Members usually elect a board of directors and officers who run the day-to-day operations of the cooperative, while regular members hold voting power and control the overall direction of the cooperative. The amount of a member’s investment does not affect the weight of each vote, so no one person can dominate the decision-making process.

**Advantages**

a. Members of a cooperative only taxed once on their income from the cooperative and not on both the individual and the cooperative level.

b. Government sponsored grant programs to help start cooperatives example USDA rural development programs.

c. Cooperative members can routinely join or leave the business without causing dissolution.

d. It is a democratic organization.
Disadvantages

a. **Slower cash flow**: usually many small investors as members.

b. Success depends on full members’ participation.

References


