LLC Creation Checklist

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Checklist for Creating a Farm Business as an LLC

For farmers starting a new business, an LLC may be the right business entity. For existing sole proprietors or general partnerships, it may be a good idea to convert to an LLC. This business entity can help farmers create clear decision-making procedures, outline responsibilities, plan an exit strategy, and manage potential liability.

This guide is intended to orient farmers who have made the careful decision to become an LLC with the basic outlines of the process. LLCs are a matter of state law and each state may have different requirements. This checklist will help famers understand the big picture. Keep reading for more information on each step.

Prepare for the LLC

- ☐ Settle on a name for your business and verify that your chosen name is available
- ☐ Verify that an LLC is the right entity for your farm business
- ☐ Prepare to allocate assets between business and personal ownership

Establish the LLC

- ☐ Draft articles of organization
- ☐ File articles of organization

Implement Best Practices in Farm Business

- ☐ Allocate assets between personal and business ownership
- ☐ Document relationships for personal assets used for farm purposes
- ☐ Update websites, brochures, invoices, order forms and other materials with the "LLC" designation, if required
- ☐ Draft an operating agreement
- ☐ Follow the operating agreement
- ☐ Make note of any annual obligations such as when, where, and how to file your annual report with the state.

This list is not exhaustive. Find further information on organizing a farm business at the Farm Commons website: www.farmcommons.org

Prepare for the LLC

- ☐ *Settle on a name for your business*

Choosing a name is a very important step for your business. A farm name helps create an identity for you, your product, and your entire foodshed. But, it's also a legal consideration. Many states will prohibit two businesses from registering the same business name in that state. In addition, if you choose the same name as another business already in operation, that business may demand that you stop using their name. If this problem comes up after a farm has been around a few years, changing the name can confuse customers. And, it's sad for the farm owner. Keep that from happening by choosing a farm name that isn't already in use. First, check state and federal databases of trademarks and trade names. Generally, the state's secretary of state office will maintain a database of business names or "trade names," which will likely be searchable online. Farms may also check the federal trademark database. A basic google search will point you in the direction of these databases. Although a farm should not automatically assume that federally registered names are unavailable, consider it a caution flag. Get more information before choosing a name already registered in the federal database. Finally, farms may want to check if their preferred website address is available and do a basic google search for existing businesses with the same name.

- ☐ *Verify that an LLC is the right entity*

Although LLCs are a popular and wise choice for many farm businesses, each farm should do their homework. Consider your state's filing fees and annual fees, the level of risk faced by the farm business, whether financing is affected, and how farm partners feel about it before creating an LLC. The decision is not necessarily complicated; it should be intentional. (As a specific caution, any farm looking to convert from a corporation to an LLC should seek the advice of an attorney before going forward. Converting from a corporation to an LLC may have undesirable tax consequences.)

- ☐ *Prepare to allocate assets between business and personal*

The essence of an LLC (or a corporation) is that the business is distinct from its owner or owners. Accordingly, owners have to follow through with that distinction in practice. This means that the owners need to decide which assets are personal and which are business. For farms, the ownership of land can be a delicate decision. Many farmers prefer to keep the land under personal ownership, and then lease their personal land to the farm business for farm usage. This allocation can affect the farm business's balance sheet. If you work with an accountant, ask them for advice. If your farm is financed through a bank or the Farm Service Agency, talk with your loan agent about any effect on your qualifications or personal loan guarantees. Although this allocation may seem overwhelming considering the large number of assets many farms have, it shouldn't be too complicated. A common sense approach is likely the best. If assets are used for the farm, they should likely be farm assets. At this point, the farm should bear in mind that this division will occur and gather any necessary information to make the transfer.

Establish the LLC

- ☐ *Draft articles of organization*
- ☐ *File articles of organization*

This is perhaps the easiest part of creating an LLC. Each state requires that an LLC file a document titled "Articles of Organization." Legally speaking, the articles of organization are defined by state law, which specifies exactly what information must or may be included in the articles of organization. To make things easier on business owners and the government agency processing the articles, many states provide fillable form articles of organization. Some states will require that the business use the form, while others will allow self-drafted articles. Some agencies don't provide forms at all, and in that case, farmers should simply create a document with the information requested in the statute. Filing is generally handled by the state secretary of state's office. A google search should bring up a form and more information.

The articles of organization will likely require you to list the business' "agent." An agent is a person who will accept service of process in the event that your farm is sued. Most articles of organization also require listing the business' street address and may require a listing of members. Legally speaking, a member is the owner of an LLC. Finally, the form may ask whether the entity is "member managed" or "manager managed." Which one is your farm? It depends on who has the authority to make decisions for the business. If all owners/members may make decisions (such as mortgaging the property, selling the business, etc.) the farm may be member managed. If only specific people may make those decisions, the farm may be manager managed. The information on the articles of organization may be changed by filing amended articles.

The form is generally submitted online, and a fee is likely required. Each state charges different fees, which vary between $25 to $1000. In addition, most states require an annual fee to maintain the LLC, which is generally less than the fee to create an LLC.

Implement Best Practices

☐ *Allocate assets between personal and business ownership*

As discussed above, a farm business needs to follow through on creating an LLC by making the division between business and personal. If the farm doesn't already have a separate bank account, set one up. Farm expenses and payments should move through the farm account, only. (If you forget the farm checkbook and use your personal bank card instead, you may pay yourself back, of course.) Next, determine which assets are farm and which are personal. A common sense allocation is probably the best route. This process can be quite simple- there's no need to detail every feed scoop, hand weeder, or trash bin. Making your best guess as to the value of the farm's property and placing it on the farm's balance sheet is a simple way to document the transfer.

There is no need to get creative. If a farm tried to keep all assets personal and leave the farm with nothing, a court would likely not respect the LLC at all. The allocation must be based in reality and the farm must have enough assets to capitalize the operation.

☐ *Document relationships for personal assets used for farm purposes*

If you choose to hold ownership of the land with yourself personally, you should document the new relationship with the business. If the farm business uses your property, the farm business has a lease with you, whether one is written or not. Written documents are generally the better choice, and it can be a very simple one-page outline of basic terms such as rental rate, lease term, and renewal procedures. Many individuals choose to lease the farmland for a rate equal to the value of the annual property taxes, but each farm has unique needs.

Now is a good time to discuss our objectives in allocating assets and writing leases. At any point in time, a court should be able to determine which assets are the farm's and which are personal. This is because the farm's creditors can go after business assets. Thus, we need to know what they are. The court should also be able to determine exactly how and why assets are used for both personal and business reasons. Your documentation can go a long way towards creating an efficient process. If records are a mess and there is no documentation, a court may decide for itself which assets are personal or business, and the farm loses an opportunity to influence the process.

☐ *Update websites, brochures, invoices, order forms, etc with the LLC designation*

State statutes require that a limited liability company use the LLC designation in the name of the business. This signals to potential creditors that only business assets are available to satisfy potential judgments against the business. If you don't like the look of the words or you've already invested in marketing materials, check with your secretary of state's office about registering a trade name without the letters. For invoices and other official business, it's best to include the letters after your name.

- ☐ *Draft an operating agreement*

Although not required by most state laws, an operating agreement is highly recommended. The operating agreement lays out exactly who makes decisions for the farm. It outlines how members can enter the business, leave the business, and receive distributions. The agreement also allocates business profits and losses. If a farm does not have its own operating agreement, state law provides default rules. However, those rules may not be best for the farm business. The operating agreement is the farm business's chance to establish rules and procedures that work best for the farm's individual situation.

Writing an operating agreement can be a very valuable process for farm owners, even if the state's default rules will work perfectly well. The operating agreement is a chance to think through some very important contingencies. What happens if a farm partner dies? What if one partner wants to leave the business? These problems can cause massive disruption if people haven't thought them through. The discussion process puts everyone on the same page. As we all know, sometimes the conversations we don't want to have are the ones we really need to have.

- ☐ *Follow the operating agreement*

If you go to the work to outline how the business should handle important things like decisions, taxes, and departure of a member, it's very important to follow the document. This gives the business legitimacy in court. And, if you went to all that effort, you should make it work for you.

- ☐ *Fulfill annual obligations*

Your state will likely require an annual report and an annual fee to maintain your LLC. If you neglect these duties, the state may dissolve your LLC. The Internal Revenue Service will also expect additional filings. Talk with your accountant or tax preparer, or your secretary of state's office and the IRS for more information on filing LLC taxes.