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Planning a Father-Son Farm Partnership

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planning a **father-son
farm partnership**



Summary

In this day of high mechanization, it is difficult for a young man to get started in farming. The most painless way of beginning is to gradually work into the business on the home farm. The father-and-son farm partnership provides a business-like way to make this possible.

The experiences of a number of farm families have shown that both father and son have much to gain from a successful partnership. If the arrangement is to succeed, there are a number of conditions which generally must be met. Most important of these are interest of the son in farming, ability and willingness to get along, satisfactory housing, and adequate size of business.

While there are many possible arrangements for providing the son with income from the farm, it is generally most desirable that a mature son be made a full partner in the entire business. The use of a genuine partnership is advantageous from an income tax standpoint. Partnerships involving two or more sons are both possible and workable.

When a father reaches 65, he should consider the advantages of retiring from the partnership, renting the farm to the son, and collecting social security benefits. He should also make some provisions for turning the ownership of the farm over to the son.

A written agreement is practically a "must" for a sound partnership. The agreement proposed herein can be modified as desired to suit practically any situation.

Unlike a corporation, a partnership pays no income tax. It is, however, required to make a report of its income and show the distribution to the partners, who then pay the taxes on their respective shares.

Planning a Father-Son Farm Partnership

CHARLES H. BENRUD¹

Almost one-third of the farmers in South Dakota in 1954 were over 55 years of age, according to the U. S. Agricultural Census. Many farmers find it advantageous to retire from actual farming and rent out their farms at age 65, in order to qualify for Social Security benefits. This means that a large number of new farm operators are needed each year.

At the same time, thousands of farm boys are confronted with the task of selecting their life work. Many would like to farm, but are wondering how they can ever raise the capital required. The day is past when a young man needed little more than a team of horses, a plow, and a wagon to begin as a farm renter. Today, unless he has machinery and livestock worth well into five figures, he is apt to have a hard time succeeding.

The problem of getting the new operator established is currently being met by many farm families through father and son farm partnership agreements. Such agreements are making it possible for the son who wants to farm to gradually buy his way into the farm business, so that he will be in a position to

take over when his father retires. Where there is no son who is interested in farming, often a son-in-law is taken into the business. There are also instances where an unrelated young man has been taken in as a partner.

In any case, most of the time both partners benefit from a partnership arrangement. The combination of an established farm business, the experience and wisdom of the senior partner, and the ambition and energy of the junior partner generally makes for a profitable enterprise. The older man can accumulate funds for retirement at the same time that the young man acquires equity in the capital needed to operate the farm.

Starting a farm partnership involves a number of important considerations, both personal and economic. The purpose of this circular is to help farm families in setting up workable father-son agreements. It attempts first of all to outline the basic requirements for successful partnerships, and secondly to provide suggestions to assist in working out satisfactory arrangements.

¹Associate Economist, South Dakota Agricultural Experiment Station.

What Makes the Farm Partnership Succeed?

The experiences of a large number of farm families have shown that there are several factors which are quite important in contributing to the success of a father-son partnership. Those which are generally considered to be essential are as follows:

A. Personal Considerations

1. Desire of the son and his wife to farm.
2. Ability and willingness to get along.
3. Satisfactory living conditions for two families.
4. Belief that a partnership is advantageous to both parties.
5. Knowledge of farming by the son.

B. Economic Considerations

1. Adequate size of business.
2. Good farm management.
3. Complete and accurate farm records.
4. Partnership in the entire business.
5. A sound partnership agreement.

Personal Considerations

1. **Desire of the son and his wife to farm**—Life on the farm can be very rewarding. The independence of operating one's own business and the feeling of freedom involved in working outdoors are among its advantages. Working with growing crops and livestock can provide satisfactions not found elsewhere.

But farm work can be hard, and the hours long. There is the risk that the crops may fail, the pigs may get

cholera, or prices may decline. Sometimes the cows may get out when the family is getting ready to go to a party. And there are the isolation and the distance and often bad roads involved in getting to town, school, and church.

In no other occupation are the home and business tied so closely together as they are in agriculture. Whereas the factory worker needs never discuss his job at home, the topics for dinner conversation on the farm may be the crop prospects, recent price changes, or the rush season coming up. It cannot be avoided; the entire family is constantly in contact with the operation of the farm.

It is most important, then, that the son and his wife be really interested in farming and want to farm. They must be willing to make the sacrifices necessary in getting started, and to work long hours and take risks in return for the advantages involved. If they are afraid that farming would be drudgery, they had better think twice before becoming involved. Sometimes a try at city life will help them to decide definitely one way or the other.

2. **Ability and willingness to get along**—Partners in a farm enterprise must be able to work closely together. There are countless decisions to be made, and there must be "give and take" on both sides. The father must realize that his son is a grown man and allow him to make many of the decisions. Sometimes he may need to let his son go ahead

and make mistakes, in order to learn and avoid more serious ones later. He must be ready to accept new ideas and methods.

The son, on the other hand, must have faith and confidence in his father, and recognize the value of his father's experience and judgment. He must be patient when his father will not go along with a new idea. Perhaps his proposal needs to be re-examined and some changes made which will make it more certain to succeed.

In general, both of the partners and their wives must be willing to go more than halfway in order to get along. "Live and let live" is a pretty good motto to follow. Or as one son has aptly stated, "They must follow the Golden Rule and have faith."

3. Satisfactory living conditions for two families—It has been said that it is better to depend on coal, oil, or gas for heat than to get it from domestic friction. It is usually unsatisfactory for both families to live together in one household. An attempt to do so may result in a permanent disruption of good rela-

tionships. The chance is too great to be worth taking.

Perhaps there is an empty house nearby that can be rented. Sometimes in adding more land to make the business large enough another house is also added. In some cases father and son have worked together to build a new house for one family. If the farm house is quite large, it may be possible to convert it into two apartments. If so, they should be completely separate. Provision of privacy for each family is one of the most important factors in helping a partnership to succeed.

4. Belief that a farm partnership is advantageous to both parties—Both parties and their wives should be convinced that they will succeed better together than separately. Confidence in each other and in the partnership can go a long way in helping to make it successful.

5. Knowledge of farming by the son—It is quite essential that the junior partner in a farm enterprise be familiar with the business of farming. If he is to take responsi-

A separate house for each family is highly desirable.



bility and make decisions he needs a good background. Four-H Club work and agricultural courses in high school can help the future farm partner to acquire information and experience to supplement what he gains from taking part in the regular farm work. Attending a school of agriculture or an agricultural college can also help him to obtain a better insight into agriculture as a business, as well as inspire him to greater achievements.

Economic Considerations

1. Adequate size of business—

This is the most important of the economic factors. Just starting a partnership will not make the farm income large enough for two families. If there has been only enough for one family before, unless the income can be increased, two families are going to have a hard time managing. If the business is not large enough to keep two men busy and provide a good living for two families, there are several possibilities. Perhaps more land can be bought or rented. There may be land on the farm that can be drained or cleared. Or more livestock or a specialized crop enterprise may be added. In some cases the father takes on off-the-farm work such as ASC committee work or selling seed corn. In any case, if a partnership is to succeed, there must be sufficient income so that both families can live comfortably and the son can build up equity in the business.

2. Good farm management—

Good management is essential to the success of any farm business,

and a partnership is no exception. The following are generally considered to be measures of good management:

- a. Adequate size of business.
- b. Production of high - return crops.
- c. High crop yields.
- d. Suitable kinds and amounts of livestock.
- e. Good production per animal.
- f. Good man-labor efficiency.
- g. Moderate power, machinery, and building costs.

Farm record studies in South Dakota and other states have consistently shown that farms which excel in these measures of efficiency have higher than average incomes. Most of these things do not just happen. They have to be developed through careful planning on the basis of past records and the use of the basic principles of farm management. "Outlook information" can be very helpful in planning and budgeting the farm business, as can information of all kinds from the Agricultural Extension Service.

To the above list might be added:

- h. Maintenance of soil fertility.
- i. Good judgment in buying and marketing.
- j. Wise use of credit.

While not nearly so easily measurable in terms of results, these factors are obviously important. If the farm is to continue to be profitable, the productivity of the soil must be maintained. In enterprises such as livestock feeding, careful buying and selling can easily make the difference between a good profit and a sizable loss. The use of credit for

purchasing additional land and essential machinery and livestock may make the farm more profitable. However, extreme care should be exercised in buying non-essentials on credit. Before any money is borrowed, careful consideration should be given to all of the factors involved, including the risk of price drops and crop failure as well as the possibility of making a profit. Since in a partnership each partner is liable up to the full amount for all partnership debts, no debts should be entered into except by mutual consent of both parties.

3. Complete and accurate farm records—Good records are important to any farm business, but even more so to a partnership. The South Dakota Farm and Ranch Record Book is well suited to keeping the necessary records. Records are needed both for making a proper division of income and expenses and for reference for farm planning. Both partners should have access to the records and be familiar with them.

In addition to receipts, expenses, inventories, and depreciation schedules, the Farm and Ranch Record Book provides space for records of crops, livestock production, and feed for livestock. With this information, it is possible to compare the probability of the various enterprises and learn which ones are most efficient and ought to be expanded and which ones are least profitable and should be either improved or eliminated.

4. Partnership in the entire farm business—While it is an excellent



Good records are essential to the farm partnership.

prelude to a partnership for a teenage youth to begin by owning a few animals or sharing in one enterprise, such as dairy, poultry, or swine, this type of arrangement is not satisfactory on a permanent basis. If the junior partner is interested mainly in maximizing the returns from a single enterprise, he can easily tend to neglect other parts of the business. There may also be disputes as to how far this enterprise should be expanded. If a partnership is to succeed, both partners must be interested in the operation of the entire farm. For this reason, it is desirable that both share in the ownership and management of, and the income from, the entire farm business.

5. A sound partnership agreement—A sound agreement, fair to all parties involved, is a “must” for a good farm partnership. It should definitely be in writing with main essentials as follows:

(1) It should state what each partner is to contribute to the busi-

ness, and should include an itemized list and evaluation of all property brought into the partnership.

(2) It should provide for an equitable distribution of receipts and expenses.

(3) It should provide for proper

upkeep of the farm buildings and other improvements.

(4) It should be flexible enough to provide for practically any situation which might arise.

(5) It should be easily understood.

Types of Agreements in Use

Studies of father and son farm operations have disclosed many types of arrangements, no two of which are exactly alike. Not only are there many different types of rather permanent arrangements, but there are also innumerable plans for working up to a full partnership. The most common types of arrangements are:

1. "Indefinite allowance"—This plan which has been traditional in many American communities could very well be referred to as "family socialism," since it is based upon the Socialist motto, "From each according to his abilities, to each according to his needs." All farm property and income are considered to belong to the family, with each member working as hard as he can from the time he is old enough to feed the chickens and get the cows, and in turn receiving room, board, clothing, and a little money occasionally for spending on other items. There is often a tacit understanding that some assistance will be forthcoming when a son is ready to start farming, but there may be a great variation in the amount received by the different members of

the family. Often the oldest son works at home for years and gets a very modest start; a few years later his younger brother takes over the farm business at home, "lock, stock, and barrel." Another son may tire of this type of arrangement after some years and go off and get a job in town. He probably receives nothing for the labor which he has contributed. On the other hand, one or more sons or daughters may be sent through college on family funds, while the son who remains at home continues to work with no definite agreement, and when the parents die they all inherit equally. In order to be fair to all concerned, it has been suggested that some other system be worked out by the time a son is 7 years old.

2. Wage agreements—It is, of course, possible for a son to be paid wages for the work he does on the farm. This may be all right for a short time, but it does not in itself provide an opportunity for the boy to begin investing in farm property, and he cannot help feeling he is only a hired man. He acquires no real interest in the profitability of the farm business.

3. **Project agreements** — Many farm boys become interested in farming through 4-H and FFA work. Such projects provide opportunities for them to become owners of livestock and earn their own money. In return for general work on the farm, a boy is given a calf, pig, or lamb and the necessary feed. He can raise the animal, sell it, and reinvest some of the money. Or he may keep it for breeding purposes and start a herd or flock. As he gradually accumulates more livestock, he gets both experience and a start toward becoming a full partner in the farm business. This is a good practice for boys of school age.

4. **Enterprise agreements** — Another arrangement for providing the son with income is the enterprise agreement. He may be given a part or all of the returns from one entire enterprise. This is a good follow-up to the project arrangement, but still not satisfactory as a permanent proposition, since it can easily lead to his being mainly interested in one part of the farm business.

5. **Wage and income-sharing**

agreements—For the son who does not start early with project agreements, a wage and income-sharing agreement may be suitable for a time. He may receive a wage equal to or slightly less than the going wage for the community, plus a share of the net income from the farm. This will help him to be interested in keeping the costs down and maximizing returns.

This type of agreement can be used as a testing period for the son, to see whether or not his interests lie in farming. It will give him a chance to earn some money without first having some to invest. But if he is to continue on the farm, he should work into a joint-operating agreement or full partnership.

6. **Full partnerships or joint operating agreements** — Finally, there is the full partnership, or joint operating agreement, in which the father and son share in the ownership of the livestock, equipment, and supplies, in the management of the business, and in all receipts and expenses. This is the type most suited to a mature son or other junior partner.



The "50-50" Partnership

A number of bases have been used by fathers and sons in setting up partnerships involving the entire farm business. In some cases the son furnishes only his labor and management, pays one-fourth of the expenses, and receives one-fourth of the receipts. In others, he furnishes some of the operating capital in addition, and participates in income and expenses on a one-third or two-fifths basis. One disadvantage of these types of arrangements is that it is difficult to compare the relative contributions and make sure that income is equitably distributed. However they may be useful as stepping stones to a full "50-50" partnership.

The "50 - 50" partnership has proved to be a successful and popular type of arrangement. Not only does it make the son a full and equal partner with his father, but it also simplifies both record-keeping and the equitable distribution of income on the basis of contributions.

In setting up a "50-50" partnership, the son purchases a one-half interest in the farm personal property, and the father and son form a partnership, which rents the farm from the father. It may, of course, also rent additional land; the son may also purchase land and rent it to the partnership. Under this arrangement, the partners share equally in furnishing labor, capital, and management, and also in the profits. In addition, each receives cash rent on his land, if any. While this rent may be set high enough to

cover taxes, insurance, and repairs, as well as interest on the value, a common practice is to set it equal to the interest alone, and have the partnership pay all of the expenses involved. If the partnership pays for all of the major as well as minor repairs, there is usually no need to consider depreciation on the buildings. New buildings or major improvements should be paid for by the owner, and appropriate adjustments made in the rent.

The question now arises, "How is the son to acquire 50% ownership of the farm personal property?" He may have some money which he has earned in wages or from project or enterprise arrangements, and also

On a good partnership farm, the home is not forgotten. Modern kitchens help keep the wives happy with the arrangement.



some livestock from his projects, but the total value is usually only a small part of the amount needed.

It might be possible to borrow the money at the bank and pay the father for a half interest. But bank loans for the purchases of personal property usually are of the short term variety, with fairly high rates of interest. A rigid schedule of large payments is not conducive to sound sleep, especially in case of drought or low prices. In addition, the father may have no particular need for the money and may just put it in a savings bank at a much lower rate of interest.

Usually much more satisfactory, then, is for the son to give his father an interest-bearing note in part-payment for his share in the business. The long-term rate of interest on farm mortgages is probably appropriate, and part of the loan can be paid off out of the son's share of each year's income. This provides a flexible method of payment, and it entails no net interest cost to the family. In some cases, the father purchases more land to increase the size and income of the farm, and as the son pays for the personal property he makes payments on the land.

Legal and Income Tax Considerations

Some people hesitate to enter into actual legal partnerships, because of the unlimited liability of each partner for the debts of the partnership. For this reason, some writers recommend the use of "operating agreements" or "business agreements," which include the specific provision that a partnership is not being established. If, however, the agreement provides for sharing the ownership of farm property, sharing in management, and sharing in the net returns from the business, most courts would likely rule that there has been intent to create a partnership, regardless of any statement to the contrary.

It is not only possible, but also desirable, to include in the partnership agreement a clause requiring the approval of both partners of all purchases and indebtedness involv-

ing more than a certain amount. Such a clause does not, however, protect one partner against business debts incurred by the other in violation of the agreement, unless the third party involved has been informed of it. More important in this connection than legal enforcement is the mutual confidence and trust of the partners. This really ought to be found as a matter of course between a father and son who have decided to farm together. Between two non-related parties, there might be slightly more risk involved.

In addition to debts, each partner is also liable to the full extent for all "torts" of the partnership. These are actions committed in the course of the farm business for which the partnership may be required to pay damages. Farm liability insurance can be used to protect

the partners against most of this type of liability.

Actually, there is one definite advantage to be gained from a true partnership. This is because of the income-tax rule on capital gains. When a partnership is terminated, as when the father sells the son his share and retires, the partnership share is considered a capital asset and therefore only one-half of the gain involved is taxable. In addition, since capital gains are not considered earned income, the transfer can be made after the beginning of the year during which he begins to collect social security benefits, and he can stay in a fairly low tax bracket. Where, on the other hand, there has been no partnership, the sale of all grain, feed, and young and market stock is considered ordinary income and taxed on its full value. In addition, since sales of such items constitute earned income and count against social security benefits, the transaction has to be made during the final year of operation, when in combination with the regular income for the year it can easily put him in a high bracket.

A few words should also be said about current income taxes. Unlike a corporation, a partnership itself pays no income tax. It is, however, required to submit a partnership report on Form 1065. The receipts, expenses, and depreciation schedule for the farm business are entered on the usual Schedule F, the same as for an individual farmer. The ordinary income and capital gains are then entered on Form 1065, where a division of each is

made to the partners. Finally, each partner's share is entered on his individual report and he pays the tax. A partner renting land and buildings to the partnership is permitted to deduct depreciation on the buildings from the rent received.

When the partnership is started and the father sells a one-half interest in his farm personal property to the son, he must, of course, report this sale on his income tax return. As usual, the amounts received for crops, market stock, and young breeding stock (under one year) are reported as ordinary income on Schedule F, and the profits on sales of machinery, equipment, and dairy, breeding, and work stock are considered capital gains and reported on Schedule D.

Since the father's income during the first year of the partnership is apt to be lower than that received during his last year as an independent operator, he will usually find it easier to keep out of a high bracket if the sale is made in January, rather than in December. The January sale also results in postponement of the tax for one year.

What is income to the father, however, becomes a cost to the partnership. The January sale is also advantageous in this respect, since the amount paid by the son for grain and roughage can be deducted from the year's partnership receipts as "feed bought." As the market stock is sold, the amount which he has paid can also be deducted as cost, along with the father's share of any original purchase price. Depreciable items can be set

up in a partnership depreciation schedule on the basis of one half of the current value in the old schedule plus the amount paid by the son for his one-half share. On feed and the items sold during the year, the income and deductions balance out currently, and on capital items they will by the time they are sold or completely depreciated. Care must be taken in making out the tax returns, however, so that the income is distributed in such a way that the son receives the credit for the amounts which he has paid. In effect, the tax paid by the father is saved by the son.

It is, of course, possible for a partnership to report its income tax on the accrual basis. Under the cap-

ital gains rule for raised breeding stock, however, the cash basis is generally more advantageous. Where it is likely that the size of the business may be increased, this is even more the case, since increases in inventories are taxable on the accrual basis, but not on the cash basis.

It is a good idea to consult the family lawyer before entering into a partnership, in order to be sure that the agreement is properly drawn up and understood by both partners. It may also be desirable to obtain qualified assistance with the first year's income tax returns, in order to assure that the transfer and partnership income are properly handled and too much tax is not paid.

Living Arrangements Under the Partnership

Since the partnership rents the land and buildings, each partner is equally entitled to a place to live. As long as a son is single, he will no doubt continue to live with his parents. He should then pay part of the costs of food and fuel purchased. If there are no other children at home, the father and son can share all household expenses equally. This will result in the son's helping to pay for his mother's share, in return for her cooking and performing other household duties for him.

The son or other junior partner who is married is entitled to housing at least somewhat comparable to that enjoyed by the father. If there is only one house on the farm, and it is not feasible to divide it

into two apartments, it is up to the partnership to rent or otherwise provide an additional house. It may be best for the son to live on the farm and the father to move elsewhere, since in the long-run it is the son who is to be the farm operator and the opposite situation would involve extra moves. Then, too, even before actually retiring, the father will probably prefer to turn much of the responsibility for looking after the livestock over to the son.

Each partner is also entitled to a share of the food raised on the farm. While a definite accounting could be made of the amounts used by each family, and an adjustment made at the end of the year, it is a common practice to allow each to

use whatever he needs in the way of milk, eggs, and meat, with no record being kept, and also to grow his own vegetables.

Since the family cars are usually used for farm business as well as pleasure, many of the expenses for both automobiles may be paid by the partnership. One practice is to

allow each partner to use as much gasoline from the farm tank as he needs, but require him to pay out of personal funds for any that he buys at filling stations. The result is that local driving averages out pretty well, while long-distance trips are at least partly paid for by the family making them.

When the Father Retires

If the partnership has been started fairly early, and the farm is well-managed and profitable, it should be possible for the son to pay for his share in the partnership out of his earnings by the time his father reaches age 65. Then it is time for him to consider buying his father's share of the partnership and renting the land and improvements. Since the father has been "materially participating" in the farm business, the rent for his land as well as his share of the partnership income has

counted toward social security, and he and the mother (if she is 62 or older) should be eligible for sizable monthly checks.

If the son rents for cash, and the lease does not provide that the father is to "materially participate" in the operation of the farm, for social security purposes it is considered that any participation on his part is "incidental." He can therefore work for the son for up to \$1,200 a year, as well as receive rent and perhaps also some inter-

A project or enterprise arrangement is an excellent prelude to a full partnership.



est, without losing any benefits. In order to be on the safe side, it is a good policy to have a written lease, which definitely states that it **does not** provide for or involve "material participation" by the landlord in the operation of the farm.

In some cases, the father may wish to retire from actual work

before he reaches 65. To continue to build up his social security base, he can remain in the partnership and continue to participate in management until reaching that age. Compensation for the difference in labor contributions can be made by paying the son for his labor before net returns are divided.

More Than One Son

Where there are two or three sons who wish to farm, the partnership plan is still applicable. The father sells a share in the personal property to each son, as one-third to each of two, or one-fourth to each of three, and they all share equally in net income. For three or four partners a larger business is, of course, necessary. But modern large-scale machinery can often be used on many more acres than are found in the average farm, so it may be possible to rent or purchase considerably more land to add to the business, without too much extra investment in machinery, and with resulting lower costs of production.

Often in this type of arrangement when the sons buy out the father's share when he retires, they continue the business of "John S. Jones and Sons" as "Jones Bros.," in order to be able to retain the advantages of large-scale operations, joint management, and opportunities for vacations and Sundays off.

Where more than one son is to be included in the partnership, it is advantageous from an income tax standpoint to take one son in first and then a year later sell a share in the partnership to the second son. This results in taxation at the lower capital gains rates on all of the gain from the sale of the second part.

Transferring the Farm

The final step in getting a son established in farming is to arrange for him to become the farm owner. This can be done by sale or will, as the father may decide. The situation which definitely needs to be avoided is that of making no arrangements and allowing each of several sons and daughters to inherit an undivided interest in the farm. Far too many family feuds have begun over the disposition of the "home place." And far too many family farms have been sold to outsiders because the heirs could not agree on an arrangement to sell it to one of their number.

While some fathers sell their farms to their sons and proceed to live on the interest, many have found it more desirable to make use of a "conditional will," bequeathing the farm to the son who is operating it, with the requirement that he pay the other heirs each a certain amount of money to gain clear title. He may be given several years to pay them off. One advantage of this method is that the father retains control over the farm as long as he lives. Should the son die first, the father can change his will so that another son, or perhaps a daughter and son-in-law, can take over. And in any case he and the mother can continue to live on the farm as long as they wish.

Many bulletins have been written on the subject of transfer of farms from one generation to the next. It is suggested that one of these be consulted by any farmer considering arranging for such a transfer.²



High quality livestock, good management, and cooperation in decision-making are all important in helping the partnership to succeed.

Suggested Partnership Agreement

There are, of course, no definite rules as to exactly what should go into a farm partnership agreement. There is also no one specific combination of arrangements which must be followed. The following is an example agreement which may either be used "as is" or adjusted to suit a particular situation. It is generally desirable to obtain legal counsel in setting up the agreement. Having the agreement witnessed or notarized will help to make it official and binding.

Copies of this lease form are available from your county agent.

²One such publication, *Keeping Your Farm in the Family*, S. D. Agri. Exp. Sta. Bul. 398, 1950 is available at County Extension offices and at South Dakota State College.

Father and Son Farm Partnership Agreement

This partnership, to be known as _____, is entered into this _____ day of _____, 19_____, by and between _____, the father, and _____, the son, for the purpose of operating a farm business.

The term of this agreement shall be _____ year(s) from _____, 19_____ to _____, 19_____. This agreement will continue in effect from year to year thereafter until written notice of termination is given by either party on or before the _____ day of _____ before expiration of this agreement.

A. Contributions by Each Partner

1. Labor and Management. Partners shall share equally in providing labor and management, unless by mutual consent they decide otherwise. When contributions are equal, no allowance for labor and management shall be made in the distribution of earnings. When unequal, differences in such contributions shall be compensated for by paying the partner providing excess labor at the rate of \$ _____ per month. This shall be paid out of net partnership income, before the final equal division is made.

2. Personal Property. All machinery, livestock, feed, and supplies used by the farm business shall be owned in an undivided manner by the partnership. The equities of the partners in the partnership shall be equal. The father hereby sells and transfers to the son for a consideration of \$ _____, an undivided one-half share in his farm personal property, as follows:

The son hereby sells and transfers to the father, for a consideration of \$ _____ an undivided one-half share in his farm personal property as follows:

Each partner hereby turns his undivided interest in all property, as listed, over to the partnership, in return for a share in the partnership.

3. Real Estate. a. Land and buildings owned by partners shall continue to be owned individually, and shall be rented from them by the partnership, as follows:

Description	Owner	Annual rent
_____	_____	\$ _____
_____	_____	\$ _____
_____	_____	\$ _____
_____	_____	\$ _____
_____	_____	\$ _____

b. New improvements on this land shall be paid for by the owner, but appropriate adjustments in rent shall be agreed upon before work is begun.

c. Additional land may be rented by the partnership from other owners.

B. Income and Expenses

1. Receipts. Gross receipts from all sources, including sales of capital items (except real estate), as well as ordinary sales, work off the farm, and miscellaneous receipts, shall accrue to the partnership.

2. Expenses. All expenses, including taxes, insurance, repairs, and maintenance on land and buildings owned by partners and purchases of machinery and livestock, as well as ordinary operating expenses, shall be paid out of partnership funds.

3. Handling of Funds. a. A partnership checking account shall be maintained in the _____ Bank, and all farm expenses over \$ _____ shall be paid by check. Smaller amounts may be paid by partners and reimbursed from the checking account.

b. Each Partner may withdraw up to \$ _____ each month for living expenses.

4. Settlement at the End of the Year. a. Gross cash farm income shall be computed.

b. Total cash farm expenses paid to outsiders shall be computed, and subtracted from gross income.

c. Rent shall be credited to each partner renting land to the partnership.

d. Payment shall be credited to partners for excess contributions of labor.

e. Net cash income after these deductions shall be credited equally to each partner.

f. Any amount owed by the son to the father as interest on a loan shall be transferred from the son's account to the father's account.

g. The total amount withdrawn for living expenses during the year by each partner shall be computed and subtracted from his account.

h. Any amount which the son may wish to pay to the father on the principal of a loan shall be likewise transferred.

i. Each partner may draw all except \$ _____ of his share of the partnership deposit. This minimum shall be left to use for carrying on partnership business.

j. Changes in inventories shall not be considered in making the annual settlement.

C. Other Considerations

1. Farm records shall be kept in the record book. Income tax records shall be kept on the cash basis, but an inventory of livestock, feed, grain, supplies, and accounts payable and receivable shall also be taken at the end of each year, in order to provide for the analysis of the farm business.

2. No sales or purchases exceeding \$..... for any one item or \$..... for any one month shall be made by either partner without consent of the other.

3. Housing arrangements shall be as follows:

.....
.....

Each partner shall be allowed to supply his family with meat, milk, and eggs from the partnership enterprises, and to raise a garden for home use.

5. Each partner shall be entitled to use of a farm automobile for personal driving, and to use gasoline and oil from the farm supplies. All gasoline purchased at filling stations shall be paid for out of personal funds.

D. Termination of Partnership

At the termination of this partnership, if either party is to discontinue farming, the other shall have first right to buy his share at market price. If, however, both plan to continue in farming, the property may be divided between them in such manner as shall be agreeable to both.

E. Arbitration

The partners hereby agree to submit to arbitration all differences they cannot settle in regard to partnership affairs. Arbitration shall be made by a board of three men, one selected by each partner and the third by the two so selected. The decision of this board shall be binding on both partners.

In witness thereof, the parties hereto have affixed their signatures the day and year first above written.

.....
Son
.....
Son's wife
.....
Witness
.....

.....
Father
.....
Mother
.....
Witness
.....

Settlement at the End of the Year

A partnership must make a settlement at the end of each year in order to distribute the year's profits to the partners. The procedure involved can be most easily understood through the use of an example:

Example of Partnership Receipts and Expenses and Division of Income

(Based on an actual record, 1956)

Cash Receipts		Cash Expenses	
Item	Value	Item	Value
Eggs	\$ 2006	Equipment purchased	\$ 832
Dairy products	1019	Equipment repairs	310
Poultry	174	Machine hire	288
Dairy Cattle	1605	Gas and oil	571
Sheep and wool	249	Auto expense	453
Crops	8944	Electricity and telephone	128
Government payments	1050	Crop expense	1220
Refunds	162	Hired Labor	27
Other	59	Taxes	563
Total	<u>\$15,268</u>	Insurance	139
		Improvement repairs	64
		Livestock purchased	698
		Misc. Livestock expense	88
		Feed and bedding	995
		Total	<u>\$6376</u>

	Partnership account	Father's account	Son's account
Total receipts	\$15,268		
Less total expense	—6376		
Gross amount to be divided	<u>\$8892</u>		
Rent of 295A to father (@ \$6/A	—1770	\$1770	
	7122	1770	
One month extra labor by son at \$150	—150		\$150
	6972		150
Net cash income credited to partners	—6972	3486	3486
	0000	5256	3636
Interest on loan		453	—453
Net income after interest		5709	3183
Less cash withdrawals		—1800	—1800
		3909	1383
Principal payment on loan		1000	—1000
Net amount due partners		4909	383

Assuming that there was the required minimum in the checking account at the beginning of the year, the net amounts due from the year's operations may be drawn out by the partners at the close of the year.