PAVED WITH GOOD INTENTIONS: UNINTENDED IMPACTS OF FARM BILL PAYMENT LIMITATIONS ON FARM RISK MANAGEMENT AND FARM TRANSITIONS

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ABSTRACT

Farm Bill program payment limits first appeared in the Agricultural Adjustment Act of 1938 and have evolved in complexity throughout the years. The 2008 Farm Bill brought about the payment limitation explored throughout this Article by restricting limited liability entities, such as corporations and limited liability companies (LLCs), to one Farm Bill payment regardless of the number of farmers involved in the entity. The authors argue this limitation unnecessarily restricts farmers' ability to utilize the benefits of such entities, thereby limiting the ability of farmers to manage risks and restricting their options for successfully transferring the farm to the next generation. Starting with the history of Farm Bill payment limitations, this Article explores payment limitation rules under the most current Farm Bill. It then examines the implications of limiting entities to one payment limit. The authors then argue that future Farm Bills should use an "entity agnostic" approach focusing on "direct attribution" tying payment limitations directly to individual, natural persons through their Social Security numbers, regardless of the entity form used to hold and operate farm assets. Coupled with the existing adjusted gross income (AGI) and "actively engaged in farming" (AEF) eligibility rules, this approach would continue to serve most, if not all, of the policy objectives of the Farm Bill payment limitations while allowing farmers greater flexibility to manage risk and facilitate a smooth transition of farm ownership and management to the next generation.

I. How Did We Get Here? A Brief History Of Farm Bill Payment Limitations

A. The Foundations of Modern Farm Policy: 1930s–1969

The lineage of the current Farm Bill goes back to the Agricultural Adjustment Act of 1933 (1933 Farm Bill).[1] The 1933 Farm Bill aimed to help farmers achieve "parity," though that term was not used until 1938, of their purchasing power with that of the prosperous 1909–1914 period.[2] Although the 1933 Farm Bill was the genesis of modern Farm Bills, payment limitations did not appear until the Agricultural Adjustment Act of 1938 (1938 Farm Bill).[3] Law students may recognize the 1938 Farm Bill for its role in the case of *Wickard v. Filburn* and the dramatic expansion of congressional power under the Commerce Clause.[4] Farm policy historians, on the other hand, would note that Farm Bill payment limits made their first appearance in the 1938 Farm Bill at the level of $10,000 per person per year.[5]

B. The Good Times of the 1970s and the Permanence of Payment Limits: 1970–1981

Although payment limitations made their first appearance in the 1938 Farm Bill, they were not consistently a part of the Act until 1970.[6] With the Agricultural Act of 1970 (1970 Farm Bill) payment limitations reappeared and became part of every subsequent Farm Bill.[7] The 1970 Farm Bill limited payments to $55,000 per farmer ("person") per crop under the wheat, feed grain, and upland cotton programs for the 1971 through 1973 crops, for a combined limit of up to $165,000 if a farmer grew all three crops.[8] The 1970 Farm Bill defined payments to include "price-support payments, set-aside payments, diversion payments, public access payments, and marketing certificates," but did not include loans or purchases.[9] Of

1. *See generally* Agricultural Adjustment Act of 1933, Pub. L. No. 73-10, 48 Stat. 31.
2. *See generally id.*
3. Carl Zulauf, *Farm Payment Limits: History and Observation*, FARMDOC DAILY, June 21, 2012, at 1, 1, https://farmdocdaily.illinois.edu/wp-content/uploads/2018/05/fdd210612.pdf [https://perma.cc/57WE-5FAZ].
4. *See* Wickard v. Filburn, 317 U.S. 111, 128–30 (1942).
5. Zulauf, *supra* note 3, at 1.
6. *Id.*
7. *Id.*
8. Agricultural Adjustment Act of 1970, Pub. L. No. 91-524, § 101(1), 84 Stat. 1358, 1358.
9. *Id.* at § 101(2).

particular importance, the 1970 Farm Bill also directed the Secretary of Agriculture to issue regulations defining "person."[10]

The Farm Bills of the 1970s and the very early 1980s coincided with some of the most prosperous times for United States agriculture, with many producers adopting the "fencerow to fencerow" approach to commodity production.[11] The Agricultural and Consumer Protection Act of 1973 (1973 Farm Bill), perhaps in response to the rising commodity prices, reduced the payment limit to $20,000 per person per year.[12] The 1973 Farm Bill also established rules for determining whether corporations and their stockholders are separate persons when their respective ownership interests total more than 50% of the stock of the corporation.[13] Payment limits for rice producers emerged with the Rice Production Act of 1975 at $55,000 per person for the 1976 and 1977 crop years.[14] The Food and Agricultural Act of 1977 (1977 Farm Bill) made additional refinements to payment limitations, including "escalator" pricing for wheat, feed grains, and upland cotton beginning at $40,000 in 1978 and increasing to $50,000 for those crops (and rice) in the 1980 and 1981 crop years.[15]

Then, in 1980, a new character appeared in the cast of Farm Bill payment limitations: the disaster payment limit.[16] Prior to 1980, disaster payments issued under the Agricultural Act of 1949 did not have payment limits.[17] That changed when the Agricultural Adjustment Act of 1980 created a separate payment limit of $100,000 per person for disaster payments for the 1980 and 1981 wheat, feed grains, upland cotton, and rice crops.[18] The subsequent Agriculture and Food Act

10. *Id.* at § 101(4).

11. *See* Charlene C. Kwan, Note, *Fixing the Farm Bill: Using the "Permanent Provisions" in Agricultural Law to Achieve WTO Compliance*, 36 BOS. COLL. ENV'T AFFS. L. REV. 571, 580 (2009); Jason Henderson et al., *Agriculture's Boom-Bust Cycles: Is This Time Different?*, 96 ECON. REV. (KAN. CITY), no. 4, Fall 2011, at 1, 2, https://go.gale.com/ps/i.do?p=AONE&u=googlescholar&id=GALE|A301775815&v=2.1&it=r&sid=googleScholar&asid=47cc4664 [https://perma.cc/6MJ3-U89L].

12. Agriculture and Consumer Protection Act of 1973, Pub. L. No. 93-86, § 101(1), 87 Stat. 221, 221.

13. *Id.* at § 101(4), 87 Stat. at 222.

14. Rice Production Act of 1975, Pub. L. No. 94-214, § 102(13)(A), 90 Stat. 181, 186.

15. Food and Agriculture Act of 1977, Pub. L. No. 95-113, § 101(1), 91 Stat. 917, 917–18.

16. Agriculture Adjustment Act of 1980, Pub. L. No. 96-213, § 5, 94 Stat. 119, 120.

17. *See generally* Agriculture Act of 1949, Pub. L. No. 81-439, 63 Stat. 1051.

18. Agriculture Adjustment Act of 1980 § 5, 94 Stat. at 120.

of 1981 (1981 Farm Bill) maintained the $50,000 crop program and $100,000 disaster payment limitations which remained in place until the 1990 crop year.[19]

C. The Farm Crisis and Changing Views on Agricultural Risk: 1982–1996

Then came the Farm Crisis. Born out of those tumultuous times, the Food Security Act of 1985 (1985 Farm Bill) became the foundation for much of farm policy from that point forward.[20] Title X of the 1985 Farm Bill remains the basis for all Farm Bill provisions related to payment limitations; any provisions related to payment limitations in the subsequent six Farm Bills simply amended the 1985 Farm Bill.[21] Several elements of the 1985 Farm Bill remain permanent legislation and thus constitute "default" language in the event a subsequent Farm Bill lapses without an extension or a replacement bill.[22] The authorities for administering payment eligibility and limitation provisions in every Farm Bill, ad hoc legislation affecting Farm Bill programs, and ad hoc legislation generally, amend sections 1001, 1001A, 1001B, 1001C, and 1001D of the Food Security Act of 1985.[23] The provisions implementing these laws are codified in the Code of Federal Regulations (CFR).[24]

The 1985 Farm Bill maintained status quo with respect to crop program and disaster payment limitations at $50,000 and $100,000 per person respectively,[25] which was quickly amended to a $250,000 combined payment limit in 1986.[26] The USDA also used its authority under the 1985 Farm Bill to promulgate what became known as the "three-entity rule."[27] Shortly thereafter, the Omnibus Budget Reconciliation Act of 1987 brought about three payment qualification and limitation concepts that have survived in some form to today. [28] First, the Act

19. Agriculture and Food Act of 1981, Pub. L. No. 97-98, § 1101, 95 Stat. 1213, 1263.

20. *See generally* Food Security Act of 1985, Pub. L. No. 99-198, 99 Stat. 1354.

21. *Id.* at § 1001, 99 Stat. at 1444–45.

22. *Id.* at § 1016, 99 Stat. at 1447.

23. *Id.* at § 1001, 99 Stat. at 1445.

24. *See generally* 7 C.F.R. § 1400 (2023).

25. Food Security Act of 1985 § 1000, 99 Stat. at 1444–45.

26. Pub. L. 99-591, §108.

27. MEGAN STUBBS & STEPHANIE ROSCH, CONG. RSCH. SERV., R46248, U.S. FARM PROGRAMS: ELIGIBILITY AND PAYMENT LIMITS 15 (2020), https://crsreports.congress.gov/product/pdf/R/R46248 [https://perma.cc/7BW2-44UF] ("Prior to the 2008 [F]arm [B]ill, farmers were subject to the 'three-entity rule' for determining whether an individual was within annual payment limits. Under this law, a person was permitted to receive payments up to the full cap on the first farm in which the person had a substantial beneficial interest and up to half the full cap on each of two additional farms. The 2008 [F]arm [B]ill replaced this rule with direct attribution.").

28. Omnibus Budget Reconciliation Act of 1987, Pub. L. No. 100-203, 101 Stat. 1330.

allowed spouses to have their own separate payment limits if they could prove they had brought separate farming operations to the marriage and kept those operations separate.[29] Second, it significantly limited the ability of entities to qualify as separate persons with their own payment limits.[30] Finally, the Act required that producers be "actively engaged in farming" to be eligible for specific payments.[31] The accompanying House report offered the following motivation for including the actively engaged provisions in the act:

> A small percentage of producers of program crops have developed methods to legally circumvent these limitations to maximize their receipt of benefits for which they are eligible. In addition to such reorganizations, other schemes have been developed that allow passive investors to qualify for benefits intended for legitimate farming operations.[32]

D. Freedom to Farm: 1996–2001

The 1990s brought about the zenith of United States culture in music, television, and film;[33] it also saw a host of modifications to payment limits, but largely in terms of defining specific limits for specific programs. Beyond numerical adjustments, the Federal Agriculture Improvement and Reform Act of 1996 (1996 Farm Bill), sometimes called "Freedom to Farm," applied payment eligibility and limitation requirements of the 1985 Farm Bill to Loan Deficiency Payments (LDPs), Market Loan Gains (MLGs), and Production Flexibility Contract (PFC) payments.[34]

E. The Modern Era of Farm Policy and Payment Limitations: 2002–Present

The next significant change in Farm Bill payment eligibility and limitation came in the Farm Security and Rural Investment Act of 2002 (2002 Farm Bill) in the form of "means testing."[35] Under the 2002 Farm Bill, an individual or entity was not eligible to receive direct payments, counter-cyclical payments, LDPs,

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29. *Id.* at § 1303, 101 Stat. at 1330-16.

30. *Id.* at § 1001A, 101 Stat. at 1330-12.

31. *Id.* at § 1302, 101 Stat. at 1330-14.

32. H.R. REP. NO. 100-391, at 14 (1987).

33. This is an objective observation, completely unrelated to the fact that some of the authors graduated high school and attended college during this decade. It is a fact that culture was never better than when you were in high school and college.

34. *See* Federal Agriculture Improvement and Reform Act of 1996, Pub. L. No. 104-127, § 115, 110 Stat. 888, 902 (codified as amended at 7 U.S.C. § 1308).

35. *See generally* Farm Security and Rural Investment Act of 2002, Pub. L. No. 107-171, 116 Stat. 134.

MLGs, or payments under the Conservation title of the Farm Bill if the three-year average AGI of the individual or entity exceeded $2,500,000.[36] However, if an individual or entity derived more than 75% of their average AGI from farming, ranching, or forestry operations, the AGI cap did not apply.[37]

The Food, Conservation, and Energy Act of 2008 (2008 Farm Bill) largely settled the payment limitation and eligibility landscape in its current form.[38] The Act introduced the definition of "family member" as "a person to whom a member in the farming operation is related as lineal ancestor, lineal descendant, sibling, spouse, or otherwise by marriage."[39] It also defined "person" as "a natural person, and does not include a legal entity."[40] "Legal entity," in turn, is defined as "an entity that is created under Federal or State law and that[] (A) owns land or an agricultural commodity; or (B) produces an agricultural commodity."[41] These definitions functionally drew a distinction between corporations and LLCs on one hand, and partnerships and joint ventures on the other, by allowing members of partnerships and joint ventures to have their own payment limitations.[42] The 2008 Farm Bill also brought about a new way of managing payments to people and entities: direct attribution.[43] Rather than emphasizing entities directly, and simultaneously eliminating the three-entity rule, the new language traced payments made to a farmer though any entities in which they participated:

> Each payment made directly to a person shall be combined with the pro rata interest of the person in payments received by a legal entity in which the person has a direct or indirect ownership interest unless the payments of the legal entity have been reduced by the pro rata share of the person.[44]

Not to be left without numerically named concepts, the three-entity rule was replaced by the "four levels of attribution" in the 2008 Farm Bill.[45]

36. *Id.* at § 1001D(b)(1)–(b)(2), 116 Stat. at 215–16.
37. *Id.* at § 1001D(b)(1), 116 Stat. at 215–16.
38. *See generally* Food, Conservation, and Energy Act of 2008, Pub. L. No. 110-234, § 1603, 122 Stat. 923.
39. *Id.* at § 1603(b)(1)(C)(2).
40. *Id.* at §1603(b)(1)(C)(4).
41. *Id.* at § 1603(b)(1)(C)(3).
42. *See id.* at § 1603(e)(3)(B)(ii).
43. *Id.* at § 1603(e)(1).
44. *Id.* at § 1603(e)(2).
45. *Id.* at § 1603(e)(4).

4 LEVELS OF ATTRIBUTION FOR EMBEDDED LEGAL ENTITIES.—

(A) IN GENERAL.—Attribution of payments made to legal entities shall be traced through 4 levels of ownership in legal entities.

(B) FIRST LEVEL.—Any payments made to a legal entity (a first-tier legal entity) that is owned in whole or in part by a person shall be attributed to the person in an amount that represents the direct ownership in the first-tier legal entity by the person.

(C) SECOND LEVEL.—

(i) IN GENERAL.—Any payments made to a first-tier legal entity that is owned (in whole or in part) by another legal entity (a second-tier legal entity) shall be attributed to the second-tier legal entity in proportion to the ownership of the second-tier legal entity in the first-tier legal entity.

(ii) OWNERSHIP BY A PERSON.—If the second-tier legal entity is owned (in whole or in part) by a person, the amount of the payment made to the first-tier legal entity shall be attributed to the person in the amount that represents the indirect ownership in the first-tier legal entity by the person.

(D) THIRD AND FOURTH LEVELS.—

(i) IN GENERAL.—Except as provided in clause (ii), the Secretary shall attribute payments at the third and fourth tiers of ownership in the same manner as specified in subparagraph (C).

(ii) FOURTH-TIER OWNERSHIP.—If the fourth-tier of ownership is that of a fourth-tier legal entity and not that of a person, the Secretary shall reduce the amount of the payment to be made to the first-tier legal entity in the amount that represents the indirect ownership in the first-tier legal entity by the fourth-tier legal entity.[46]

In effect, the four levels of attribution rule attempted to carry out the intent of the "direct attribution" rule: that payments received directly by the individual in their own name and payments the individual indirectly received through distributions from the entities they own are directly attributed to the individual.[47] Put another way, the attribution concept was designed to prevent individuals from sidestepping payment limitations by having multiple entities receive payments up to their respective limits and then transferring those payments to the individual.[48]

46. *Id.*
47. *Id.* at § 1603(e)(1).
48. *See id.*

The next significant changes in payment limits and eligibility came with the Agricultural Act of 2014 (2014 Farm Bill).[49] United States farm policy shifted to a risk management focus under the 2014 Farm Bill by eliminating the Direct Payment program and creating the Agriculture Risk Coverage (ARC) and Price Loss Coverage (PLC) programs.[50] At the same time, the 2014 Farm Bill limited the combined payments from those programs, along with LDPs and MLGs, to $125,000 per person or legal entity.[51] It also reduced the average AGI limitation down to $900,000 per person or legal entity, excluding joint ventures and general partnerships.[52] Moreover, the 2014 Farm Bill, and the regulations promulgated thereunder, brought about the biggest changes to the definition of AEF since the first appearance of the concept in 1987, to wit:

> (a)REGULATIONS REQUIRED.—Within 180 days after the date of the enactment of this Act, the Secretary shall promulgate, with an opportunity for notice and comment, regulations—
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> > (1) to define the term ‘‘significant contribution of active personal management’’ for purposes of section 1001A of the Food Security Act of 1985 (7 U.S.C. 1308–1); and
> >
> > (2) if the Secretary determines it is appropriate, to establish limits for varying types of farming operations on the number of individuals who may be considered to be actively engaged in farming with respect to the farming operation when a significant contribution of active personal management is the basis used to meet the requirement of being actively engaged in farming under section 1001A of the Food Security Act of 1985 (7 U.S.C. 1308–1) by an individual or entity.
>
> (b) CONSIDERATIONS.—In promulgating the regulations required under subsection (a), the Secretary shall
>
> consider —
>
> > (1) the size, nature, and management requirements of each type of farming operation;
> >
> > (2) the changing nature of active personal management due to advancements of farming operations; and
> >
> > (3)the degree to which the regulations promulgated pursuant to subsection (a) will adversely impact the long-term viability of the farming operation.

49. *See generally* Agricultural Act of 2014, Pub. L. No. 113-79, 128 Stat. 649.
50. *Id.* at § 1101, 1116–1117, 128 Stat. at 658, 668–72.
51. *Id.* at § 1603(a), 128 Stat. at 705.
52. *Id.* at § 1605(a)(2), 128 Stat. at 707.

> (c) FAMILY FARMS.—The Secretary shall not apply the regulations promulgated pursuant to subsection (a) to individuals or entities comprised solely of family members (as that term is defined in section 1001(a)(2) of the Food Security Act of 1985 (7 U.S.C. 1308(a)(2))).
>
> (d) MONITORING.—The regulations promulgated pursuant to subsection (a) shall include a plan for monitoring the status of compliance reviews for whether a person or entity is in compliance with the regulations.[53]

The USDA responded with a significant expansion of its rules governing AEF. The newly promulgated rules only applied to non-family joint ventures and general partnerships seeking to have more than one person qualify as AEF by providing significant active personal management or a significant contribution of active personal labor and active personal management.[54] Though AEF is discussed in greater detail below, it is worth noting here that the rules promulgated under the 2014 Farm Bill included several significant changes. First, the 2014 Farm Bill included a revised definition of "active personal management" contribution.[55] Next, it encompassed a quantifiable standard for determining what constitutes "significant contribution of active personal management" and "significant contribution of the combination of active personal labor and active personal management."[56] Third, it included language restricting the number of members of a non-family joint operation that may qualify as actively engaged in farming based on a significant contribution of active personal management or a significant contribution of active personal labor and active personal management to the farming operation.[57] Fourth, a member's contribution of active personal management, or of active personal labor and active personal management, to a farming operation qualifies only that specific member as actively engaged in farming and with a separate payment limitation.[58] Finally, requirements to maintain a management record of all eligible management activities performed by

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53. *Id.* at § 1604(a)–(d), 128 Stat. at 706.

54. *Id.* at § 1604(a)–(c), 128 Stat. at 706; *see also Actively Engaged in Farming*, U.S. DEP'T OF AGRIC. FARM SERV. AGENCY (Oct. 2, 2023, 7:31 AM), https://www.fsa.usda.gov/programs-and-services/payment-eligibility/actively-engaged/index [https://perma.cc/SQF9-C226] (select the "Significant Contributions Definitions" tab).

55. *Actively Engaged in Farming*, *supra* note 54.

56. 7 C.F.R. § 1400.601(b) (2023).

57. U.S. DEP'T OF AGRIC. FARM SERV. AGENCY, PAYMENT ELIGIBILITY AND PAYMENT LIMITATIONS 1 (2019) [hereinafter PAYMENT ELIGIBILITY AND PAYMENT LIMITATIONS], https://www.fsa.usda.gov/Assets/USDA-FSA-Public/usdafiles/FactSheets/2019/payment_eligibility_and_payment_limitations-fact_sheet_b.pdf [https://perma.cc/U3BF-XZJ2].

58. *Id.*

each member of a farming operation in which more than one member is making a significant contribution of active personal management or of active personal labor and active personal management.[59]

This brings us to the most current Farm Bill, the Agriculture Improvement Act of 2018 (2018 Farm Bill). Again, several modifications were made to payment limitations for various programs, including decoupling payment limits for MLGs and LDPs.[60] The 2018 Farm Bill also added "first cousin, niece, [and] nephew" to the definition of a family member, thereby bringing the definition to its current form: "[t]he term 'family member' means a person to whom a member in the farming operation is related as lineal ancestor, lineal descendant, sibling, first cousin, niece, nephew, spouse, or otherwise by marriage."[61]

II. The Current State Of Farm Bill Payment Limitations: Eligibility, "Actively Engaged In Farming," And Limitations For Persons And Limited Liability Entities

Under the current rules, there are three steps to analyze an individual's or entity's ability to qualify for payments and any limitations on such payments: (1) identify the participants; (2) determine eligibility; and (3) determine applicable limitations.[62]

A. Identify Participants

The first step to analyzing payment limits is to identify the potential program participant.[63] To do so, each person and entity involved must provide: a name, address, and either Social Security number (SSN), Tax Identification Number (TIN), or Employer Identification Number (EIN), along with additional information as required by Forms CCC-901 and CCC -902.[64] Identifying all the people or entities involved is key to analyzing the remaining considerations under the payment limit rules. It is essential to identify everyone involved in the farm operation, their spouse, any entities owned by the operation or by involved individuals, and any entities that own any portion of the operations.[65]

59. *Id.*
60. Payment Eligibility and Payment Limitations, *supra* note 57, at 4.
61. 7 U.S.C. § 1308(a)(2).
62. *See* 7 U.S.C. § 1308(e). *See generally* Agricultural Improvement Act of 2018, Pub. L. No. 115-334, § 1703, 132 Stat. 3390, 4526–27.
63. *See* 7 U.S.C. § 1308(e). *See generally* Agricultural Improvement Act of 2018 § 1703.
64. 7 U.S.C. § 1308-1(a)(1)–(2).
65. *See generally* 7 U.S.C. § 1308-1.

After identifying each potential participant, they are categorized.[66] There are three primary categories of potential program participants: (1) individuals; (2) general partnerships/joint ventures; and (3) legal entities (including corporations and LLCs).[67] A list of contributions should be created for all partners, members, general partnerships, joint ventures, and legal entities to aid in the attribution analysis that may come later.[68]

B. Determine Eligibility

The threshold question when analyzing a person or entity's right to receive financial assistance from a farm program is to determine whether they are eligible for such assistance.[69] Eligibility for assistance depends on two tests: AGI limits and AEF determinations.[70] Potential participants must qualify under both tests to be eligible to receive a program payment from the USDA.[71]

1. Adjusted Gross Income (AGI) Limit

Under the current Farm Bill, a person or entity must have an AGI of less than $900,000 to be eligible for certain program payments.[72] For purposes of the test, an individual or entity's AGI consists of the average of their AGI from the previous three-year period excluding the most recent complete tax year.[73] For example, qualification for farm program payments in 2023 would derive from the average AGI for 2019, 2020, and 2021.

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66. 7 U.S.C. § 1308-1(b)(2).

67. *Id.*

68. 7 U.S.C. § 1308-1(b)(2)(B)–(C).

69. 7 U.S.C. § 1308(e)(1).

70. 7 U.S.C. § 1308(b)(1); *Adjusted Gross Income*, U.S. DEP'T OF AGRIC. FARM SERV. AGENCY (Oct. 27, 2023, 11:00 AM), https://www.fsa.usda.gov/programs-and-services/payment-eligibility/adjusted-gross-income/index [https://perma.cc/2YML-WK28].

71. 7 U.S.C. § 1308-1(b)(1); *Average Gross Income, supra* note 70.

72. U.S. DEP'T OF AGRIC. FARM SERV. AGENCY, THE 2018 FARM BILL — WHAT IS NEW AND WHAT HAS CHANGED (Oct. 2, 2023, 4:17 PM), https://www.farmers.gov/sites/default/files/documents/FSA-FarmBill2018_WhatsChanged-19.pdf#:~:text=Average%20Adjusted%20Gross%20Income%20%28AGI%29%20AGI%20compliance%20provisions,FSA%20and%20the%20Natural%20Resources%20Conservation%20Service%20%28NRCS%29 [https://perma.cc/E8JL-W7W9].

73. 7 C.F.R. § 1400.3(b)(iv) (2023).

For individuals, AGI is the amount reported on certain tax documents to the IRS.[74] For entities, the *Payment Limitation, Payment Eligibility, and Average Adjusted Gross Income* handbook sets forth a comparable formula to calculate AGI.[75] Significantly, the AGI requirement for legal entities applies to both the entity itself and the members of the entity.[76] For example, if an entity's AGI was less than $900,000, but one of its members had an AGI of $1 million, the Farm Service Agency (FSA) would reduce the payment limit by the ownership percentage of the ineligible member.[77]

Program participants are required to verify their AGI annually with the USDA by completing a CCC-941 certification.[78] A person with an AGI exceeding $900,000 is ineligible to participate in various programs, including: PLC, ARC, MLGs, LDPs, the Noninsured Crop Disaster Assistance Program (NAP), the Emergency Assistance for Livestock, Honeybees and Farm-Raised Fish Program (ELAP), the Livestock Forage Program (LFP), the Livestock Indemnity Program (LIP), the Tree Assistance Program (TAP), and conservation programs.[79] The 2018 Farm Bill retained provisions from the 2008 Farm Bill allowing waiver of AGI requirements in cases involving conservation programs that protect environmentally sensitive land on a case-by-case basis.[80]

2. Actively Engaged in Farming (AEF)

The second program payment eligibility requirement is that a participant, whether an individual, partnership, or legal entity, must be "actively engaged in farming with respect to the operation."[81] The AEF requirements envisioned in the *Farm Program Payments Integrity Act* were codified in the *Omnibus Budget Reconciliation Act of 1987*.[82] The accompanying House Report offered the

74. U.S. DEP'T OF AGRIC. FARM SERV. AGENCY, FSA HANDBOOK: PAYMENT LIMITATION, PAYMENT ELIGIBILITY, AND AVERAGE ADJUSTED GROSS INCOME ¶ 467 at 8-3 (2023) [hereinafter FSA HANDBOOK], https://www.fsa.usda.gov/Internet/FSA_File/6-pl_r00_a03.pdf [https://perma.cc/P2G7-5JF4].

75. *Id.* ¶ 489, at 8-74.

76. *See id.* ¶ 474, at 8-28.

77. *Id.*

78. *Id.* ¶ 468, at 8-3.

79. RANDY SCHNEPF & MEGAN STUBBS, CONG. RSCH. SERV., IF11165, 2018 FARM BILL PRIMER: PROGRAM ELIGIBILITY AND PAYMENT LIMITATIONS 1 (2019), https://crsreports.congress.gov/product/pdf/IF/IF11165/2 [https://perma.cc/TB4R-8D9T].

80. *Id.*

81. 7 C.F.R. § 1400.201(a) (2023).

82. *See* Omnibus Budget Reconciliation Act of 1987, Pub. L. No. 100-203, § 1302, 101 Stat. 1330-14 (codified as amended at 7 U.S.C. § 1308-1).

following motivation for including the AEF provisions in the *Omnibus Budget Reconciliation Act of 1987*:

> A small percentage of producers of program crops have developed methods to legally circumvent these limitations to maximize their receipt of benefits for which they are eligible. In addition to such reorganizations, other schemes have been developed that allow passive investors to qualify for benefits intended for legitimate farming operations.[83]

Under the current test, a participant must meet four requirements to be considered AEF.[84] First, the participant must make a significant contribution to the farming operation of capital, equipment, land, or a combination of capital, equipment, or land (known as "left-hand contributions").[85] Second, a participant must make a significant contribution to the farming operation of active personal labor, active personal management, or a combination of active personal labor and active personal management (known as "right-hand contributions").[86] Third, the share of the gains or losses from the farming operation must be proportional with the person or entity's contributions to the operation.[87] Fourth, their contributions to the farming operation must be at risk for loss, with the level of risk commensurate with the person or entity's claimed portion of the farming operation.[88]

a. Contribution of Capital, Equipment, or Land

Both individuals and entities must independently make a significant contribution of capital, equipment, or land, or a combination of capital, equipment, or land, to the farming operation,[89] with each of these categories specifically defined by regulation.[90] Capital is "the funding provided by a person or legal entity to the farming operation for the operation to conduct farming activities."[91] To determine "whether a person or legal entity has independently contributed capital, in the form of funding, to the farming operation, the capital must have been derived from a fund or account separate and distinct from that of any other person or legal entity with an interest in the farming operation."[92] The capital contribution "must

83. H.R. REP. NO. 100-391, at 14 (1987).
84. 7 U.S.C. § 1308-1(b)(1)–(2).
85. 7 U.S.C. § 1308-1(b); FSA HANDBOOK, *supra* note 74, ¶ 141(B), at 4-1.
86. 7 U.S.C. § 1308-1(b)(2).
87. 7 U.S.C. § 1308-1(b)(2)(A)(ii).
88. 7 C.F.R. § 1400.201(b), 1400.202(a) (2023).
89. 7 C.F.R. § 1400.202(a)(1)(i) (2023).
90. *See* 7 C.F.R. § 1400.3 (2023).
91. *Id.*
92. *Id.*

be a direct out-of-pocket input" and "does not include any advance program payments" or "the value of any labor or management that is contributed to the farming operation or any outlays for land or equipment."[93] Individuals or entities may borrow capital contributions contributed directly to the farming operation.[94] This does not apply to capital contributions acquired through "a loan made to, guaranteed, co-signed, or secured by any other person, joint operation, or legal entity that has an interest in the farming operation."[95] Examples of providing capital include "funds used to pay for operating expenses such as seed, chemical, fertilizer, fuel, and repairs."[96] Capital contributions do not include "the value of labor or management" or any "outlays for land or equipment."[97]

"Equipment means the machinery and implements needed by the farming operation to conduct [the operation's] activities . . . including machinery and implements [used] in land preparation, planting, cultivating, harvesting, or marketing of the crops involved."[98] This "also includes machinery and implements needed to establish and maintain conserving cover crops on CRP acreages and those needed to conduct livestock operations."[99] Additionally, leased equipment, leased from any source, also qualifies as equipment.[100] However, leasing said equipment from another person or entity with an interest in the farming operation requires payment at a fair market value rate.[101] Irrigation equipment, if commonly used in the area, may qualify as equipment if it is not permanent in nature.[102] Custom services, including equipment, do not qualify towards "a significant contribution" of equipment except in certain situations such as cash rent.[103]

"Land means farmland [meeting] the specific requirements of the applicable program."[104] The FSA Handbook states land includes "cropland, pastureland, wetland, or rangeland that meets the specific requirements of the applicable program."[105] As with equipment, land leased from any source qualifies as land.[106]

93. *Id.*
94. 7 C.F.R. § 1400.202(c).
95. *Id.*
96. FSA HANDBOOK, *supra* note 74, ¶ 144, at 4-4.
97. *Id.*
98. 7 C.F.R. § 1400.3(b) (2023).
99. *Id.*
100. *Id.*
101. *Id.*
102. FSA HANDBOOK, *supra* note 74, ¶ 145, at 4-6.
103. *Id.* ¶ 144, at 4-4.
104. 7 C.F.R. § 1400.3(b).
105. FSA HANDBOOK, *supra* note 74, ¶ 146, at 4-9.
106. 7 C.F.R. § 1400.3(b).

Leasing land from "another person or legal entity with an interest in the farming operation [requires payment] at a fair market value."[107] Notably, "share-rented land is [considered] a contribution of the landlord, not the share-renter."[108]

For the contribution to be deemed "significant" as required by statute, the value of the land, capital, or equipment must be "at least 50 percent of the person's or legal entity's commensurate share" of one of three totals: (1) the value of the "capital necessary to conduct the farming operation"; (2) the "rental value of the land necessary to conduct the farming operation"; or (3) the "rental value of the equipment necessary to conduct the farming operation."[109] If the contribution consists of a combination of capital, equipment, and land the combined contribution must be equal to at least 30% of the person's or entity's commensurate share in the total value of the farming operation.[110]

To determine an individual's or entity's engagement by contribution of capital, equipment, or land, the USDA considers three factors:

> (1)A separate and distinct interest in the land, crop, and livestock involved in the farming operation;
>
> (2) The demonstration of separate and total responsibility for the interest in the land, crop, and livestock in the farming operation; and
>
> (3) All funds and business accounts of the farming operation are separate from that of any other person or legal entity.[111]

b. Active Personal Labor & Active Personal Management

Next, the individual or entity seeking to qualify for a payment limit must prove they make a significant contribution of active personal labor, active personal management, or a combination thereof.[112] These contributions, in FSA parlance, are called right-hand contributions.[113]

The FSA handbook notes that it can be difficult to apply these rules to farming operations.[114] "It is difficult to measure a significant management

107. 7 C.F.R. § 1400.3(b).
108. FSA HANDBOOK, *supra* note 74, ¶ 142, at 4-2.
109. *Id.*
110. *Id.*
111. 7 C.F.R. § 1400.201(c) (2023).
112. 7 C.F.R. § 1400.201(b)(ii).
113. FSA HANDBOOK, *supra* note 74, ¶ 141, at 4-1.
114. *Id.* ¶ 148, at 4-13. Something of an understatement.

contribution [because] [t]he required hours of labor will be different" depending on the type of farming operation, and it can be "difficult to distinguish between labor and management."[115]

To determine if a person or entity is "independently and separately contributing a significant amount of active personal labor or active personal management," the USDA considers:

> (1) The types of crops and livestock produced by the farming operation;
>
> (2) The normal and customary farming practices of the area;
>
> (3) The total amount of labor and management necessary for the farming operation in the area; and
>
> (4) Whether the person or legal entity receives compensation for the labor and management activities.[116]
>
> "If a member of a joint operation receives a guaranteed payment" for providing labor or management, the USDA excludes "all of the specific types of contributions for which payment is received."[117]

c. Active Personal Labor

Interestingly, the USDA's regulations do not define "active personal labor."[118] Instead, the regulations simply state that active personal labor provided by a person must be the smaller of the following: "(A) 1,000 hours per calendar year; or (B) 50 percent of the total hours that would be necessary to conduct a farming operation that is comparable in size to such person's or legal entity's commensurate share in the farming operation."[119] The FSA manual provides the following list of qualifying activities: (1) physical activities "involved in land preparation, planting, cultivating, harvesting, and marketing of agricultural commodities"; (2) physical activities "required to establish and maintain conserving cover crops or conserving use acreages"; and (3) physical activities "required in livestock operations."[120]

115. *Id.*
116. 7 C.F.R. § 1400.201(d).
117. FSA HANDBOOK, *supra* note 74, ¶ 147, at 4-12.
118. *See* 7 C.F.R. § 1400.3(b) (2023).
119. *Id.*
120. FSA HANDBOOK, *supra* note 74, ¶ 147, at 4-11.

d. Active Personal Management

The law defines active personal management as making a significant contribution of management activities to the farm operation "performed under one or more of the following categories":

> (1) Capital, which includes:
>
> (i) Arranging financing and managing capital;
>
> (ii) Acquiring equipment;
>
> (iii) Acquiring land or negotiating leases;
>
> (iv) Managing insurance; and
>
> (v) Managing participation in USDA programs;
>
> (2) Labor, which includes hiring and managing of hired labor; and
>
> (3) Agronomic and marketing, which includes:
>
> (i)Selecting crops and making planting decisions;
>
> (ii) Acquiring and purchasing crop inputs;
>
> (iii) Managing crops . . . and making harvesting decisions; and
>
> (iv) Pricing and marketing of crop production.[121]

The FSA Handbook defines active personal management as providing "general supervision and direction of activities and labor involved in the farming operation" and "services, whether formed on-site or off-site, reasonably related and necessary to the farming operation."[122] This includes:

> supervision of activities necessary in the operation[;]
>
> business-related actions that involve discretionary decision making[;]
>
> evaluation of the financial condition or needs of the farming operation[;]
>
> assistance in structuring or preparing financial reports or analyses for the farming operation[;]
>
> consultations in or structuring of business-related financing arrangements for the farming operation[;]

121. *See* 7 C.F.R. § 1400.3(b).
122. FSA HANDBOOK, *supra* note 74, ¶ 147, at 4-11.

> marketing and promoting agricultural commodities produced by the farming operation[;]
>
> acquiring technical information used in the farming operation[;]
>
> [and] any other management functions necessary to conduct the farming operation and for which the operation would ordinarily be charged a fee.[123]

The rules governing whether active personal management qualifies as a "significant contribution" differ depending on the situation. For farming operations comprised of only family members,[124] to qualify as significant contributions the management activities must be "critical to the profitability of the farming operation, taking into consideration the person's or legal entity's commensurate share in the farming operation."[125] No limit exists on the number of members who may qualify as being actively engaged in management for a family operation.[126]

For joint operations and legal entities comprised of non-family members, the active personal management must be "on a regular, continuous, and substantial basis to the farming operation," and the manager must either: "[p]erform[] at least 25 percent of the total management hours required for the farming operation on an annual basis; or . . . [p]erform[] at least 500 hours of management annually for the farming operation."[127]

Further, there are limitations on the number of members who may qualify as being engaged in active personal management for non-family entities.[128] Farming operations involving non-family members are generally limited to a single person who may qualify as "providing a significant contribution of active personal management, or a significant contribution of the combination of active personal labor and active personal management."[129] Certain operations may be allowed to qualify up to three people as providing a significant contribution of active personal management if they are deemed "large" or "complex."[130] A large operation may qualify one additional person as providing a significant contribution of active

123. *See id.* ¶ 147, at 4-11–4-12.

124. *See* 7 C.F.R. § 1400.3(b), defining family member as "a person to whom another member in the farming operation is related as a lineal ancestor, lineal descendant, sibling, first cousin, niece, nephew, spouse or otherwise by marriage."); FSA HANDBOOK, *supra* note 74, ¶ 222, at 5-75 (defining family member).

125. 7 C.F.R. § 1400.3(b).

126. 7 C.F.R. § 1400.602(a) (2023).

127. 7 C.F.R. § 1400.601(b) (2023).

128. 7 C.F.R. § 1400.602(a).

129. 7 C.F.R. § 1400.602(a)(2).

130. 7 C.F.R. § 1400.602(a)(2)–(3).

personal management.[131] The regulations consider an operation large if it: "(i) [p]roduces or markets crops on 2,500 acres or more of cropland; (ii) [p]roduces honey with more than 10,000 hives; or (iii) [p]roduces wool with more than 3,500 ewes."[132] Further, an operation deemed complex may qualify one additional person as providing a significant contribution of active personal management.[133] The regulations provide this determination shall be made by the FSA state committee and "must be reviewed and DAFP must concur with that determination."[134] The operation must provide information to the state FSA committee on the "[n]umber and type of livestock, crops, or other agricultural products produced and marketing channels used; and . . . [the] [g]eographical area covered."[135]

e. Combination of Active Personal Labor and Active Personal Management

A separate standard exists for those seeking to qualify based upon a combination of active personal labor and active personal management.[136] Again, there is a distinction between the test for entities made up entirely of family members and for non-family entities.[137]

The USDA provides that entities made up entirely of family members can use a combination of active personal labor and active personal management if that combination results in a critical impact on the profitability of the farming operation.[138] The profit amount must at least equal the significant contribution of active personal labor or active personal management when considered alone.[139] In no situation can a non-family operation qualify more than three persons as providing a significant contribution of active personal management or a significant contribution of the combination of active personal labor and active personal management.[140]

131. 7 C.F.R. § 1400.602(a)(2).

132. 7 C.F.R. § 1400.602(a)(2)(i)–(iii).

133. 7 C.F.R. § 1400.602(a)(3).

134. *Id.*

135. *Id.*

136. Payment Limitation and Payment Eligibility; Actively Engaged in Farming, 80 Fed. Reg. 78119, 78123 (Dec. 16, 2015).

137. RANDY SCHNEPF, CONG. RSCH. SERV., R44656, USDA'S ACTIVELY ENGAGED IN FARMING (AEF) REQUIREMENT 12 (2019), https://crsreports.congress.gov/product/pdf/R/R44656/7 [https://perma.cc/2QG7-VR3S].

138. 7 C.F.R. § 1400.3(b) (2023).

139. *Id.*; *see also* FSA HANDBOOK, *supra* note 74, ¶ 147, at 4-12. This combination can be used when neither the contribution of active personal labor nor active personal management alone meet the requirements of significant contribution.

140. 7 C.F.R. § 1400.602(d).

For entities including non-family members, the required significant contribution of the combination of active personal labor and active personal management means a contribution of each that: "(i) [i]s critical to the profitability of the farming operation; (ii) [i]s performed on a regular, continuous, and substantial basis; and (iii) [m]eets the required number of hours [in the table below].”[141]

Table 1 to Paragraph (iii) of the Definition of Significant Contribution of the Combination of Active Personal Labor and Active Personal Management

Combination of active personal labor and active personal management minimum requirement for a significant contribution		
Management contribution in hours	**Labor contribution in hours**	**Meets the minimum threshold for significant contribution, in hours**
475	75	550
450	100	550
425	225	650
400	250	650
375	375	750
350	400	750
325	425	750
300	550	850
275	575	850
250	600	850
225	625	850
200	650	850
175	675	850
150	800	950
125	825	950
100	850	950
75	875	950
50	900	950
25	925	950

141. 7 C.F.R. § 1400.601(b) (2023).

f. Share in Profits or Losses

Next, a person or entity must have "a share of the profits or losses from the farming operation commensurate with the person's or legal entity's contributions to the operation."[142] The FSA handbook states that total contributions that "are 'within reason' of being equal to the claimed share of profits and losses must be considered commensurate."[143]

g. Contributions at Risk for Loss

Finally, an individual or entity's "contributions to the farming operation [must be] at risk for loss, with the level of risk being commensurate with [their] claimed share of the farming operation."[144] The FSA Handbook describes this "at risk" requirement as requiring there to be "a possibility that the producer could suffer loss."[145]

h. Exceptions

The regulations provide two key exceptions to the AEF rules. First, "[i]f one spouse, or an estate of a deceased spouse, is determined to be actively engaged in farming [,] . . . the other spouse is considered [actively engaged]" without making a separate, additional contribution of management or labor.[146]

Second, in certain instances, the USDA considers landowners making a significant contribution of owned land to the farming operation as actively engaged in farming.[147] Specifically, a landowner contributing land may qualify as actively engaged if they:

> (1) [receive] rent or income for the use of the land based on the land's production or the operation's operating results;
>
> (2) [have] a share of profits or losses from the farming operation commensurate with the landowner's contributions to the operation; and

142. 7 C.F.R. § 1400.201(b)(2) (2023).
143. FSA HANDBOOK, *supra* note 74, ¶ 150, at 4-15.
144. 7 C.F.R. § 1400.201(b)(3).
145. FSA HANDBOOK, *supra* note 74, ¶ 151, at 4-18.
146. 7 C.F.R. § 1400.202(b) (2023).
147. 7 C.F.R. § 1400.207(a)(1) (2023).

> (3) [make] contributions to the farming operation that are at risk for a loss, with the level of risk being commensurate with the landowner's claimed share of the farming operation.[148]

In other words, a landowner may substitute the requirement of receiving rent or income from the land based on its production or operating results for the actively engaged requirement.[149] This applies to landowners who own an undivided interest in land[150] and to landowners who are members of a joint operation that holds title to land so long as documentation showing that "upon dissolution of the joint operation, the title to the land owned by the joint operation will revert to the member" is provided.[151]

C. Conservation Compliance

Additionally, to qualify for certain benefits, producers must be in compliance with the "highly erodible land conservation (sodbuster) and wetland conservation (swampbuster)" provisions under the 1985 Farm Bill.[152] As of 2014, conservation compliance is also required to qualify for federal crop insurance premium subsidies.[153] Essentially, a producer must agree "to maintain a minimum level of conservation on highly erodible land and not to convert or make production possible on wetlands."[154]

D. Applicable Payment Limitations

Once a potential recipient successfully meets the AGI and AEF tests, their specific payment limitations must be determined.[155]

1. Number of Payments

The number of payments an operation may receive is dependent upon the legal structure of the operation.[156] Although agricultural operations are structured in a variety of ways for program payment limitation purposes, they can be divided

148. 7 C.F.R. § 1400.207(a)(1)–(3).

149. *See id.*

150. 7 C.F.R. § 1400.207(a).

151. 7 C.F.R. § 1400.207(b).

152. MEGAN STUBBS, CONG. RSCH. SERV., R42459, CONSERVATION COMPLIANCE AND U.S. FARM POLICY 1 (2016), https://crsreports.congress.gov/product/pdf/R/R42459/27 [https://perma.cc/5FGM-68RL].

153. Agricultural Act of 2014, Pub. L. No. 113-79, § 2611(a)(1)(E), 128 Stat. 649, 762.

154. SCHNEPF & STUBBS, *supra* note 79.

155. *See id.* at 2.

156. *See id.* at 1.

into three categories: (1) individual; (2) general partnership/joint venture; and (3) legal entities (including limited liability companies and corporations).[157]

a. Individual

For a qualifying individual operating as a sole proprietor, one payment limit is available.[158] If the individual is married, then his or her spouse may also qualify, making the couple potentially eligible for two payment limits.[159]

b. General Partnership/Joint Venture

Each qualifying member of a general partnership or joint venture may receive his or her full payment limit under the applicable programs.[160] In other words, the USDA regards each member as separate for purposes of payment limitations and calculates payment limits by multiplying the number of members meeting the AGI and AEF requirements by the payment limit of the specific program.[161] For example, a general partnership with three members could qualify for three payment limits, assuming each of the members were eligible.

c. Legal Entities

A legal entity may only qualify for a single payment limit, regardless of the number of members that individually qualify as eligible for payment limits.162 This seemingly innocuous sentence forms the crux of this entire Article. Thus, the authors wish to explore it a bit further. Recall the 2008 Farm Bill defined a legal entity as "an entity that is created under Federal or State law that—(A) owns land or an agricultural commodity; or (B) produces an agricultural commodity."163 Functionally, this means the USDA regards LLCs and corporations as legal entities.164 The current statutory language then limits a legal entity to one payment limit, for example: "[t]he total amount of payments received, directly or indirectly, by a person or legal entity (except a joint venture or general partnership) for any crop year . . . may not exceed $125,000."165 Thus, a farming operation organized

157. *Id.*
158. *See* 7 C.F.R. § 1400.1(f) (2023).
159. *See* 7 C.F.R. § 1400.202(b) (2023).
160. 7 C.F.R. § 1400.106(b) (2023).
161. FSA HANDBOOK, *supra* note 74, ¶ 467, at 8-3.
162. *See* 7 C.F.R. § 1400.1(f).
163. Food, Conservation, and Energy Act of 2008, Pub. L. No. 110-234, §1603(b)(1)(C), 122 Stat. 923, 1002.
164. *Id.*
165. 7 U.S.C. § 1308(b).

as a legal entity can only receive one payment limit even though it might be entitled to as many payment limits as it has members.

2. Amount of Payment

The amount an individual qualifying for a payment may receive depends upon the specific program at issue and the total amount of payments received by the individual.[166]

a. Specific Program Limits

Some programs fall under a joint payment limit of $125,000 per year.[167] This includes Title I programs such as ARC and PLC.[168] Other programs have different limits such as $200,000 for the Conservation Stewardship Program (CSP) and $450,000 for the Environmental Quality Incentives Program (EQIP).[169] The regulations contain the following summary of payment limits by program:

166. 7 C.F.R. § 1400.1(f).
167. *Id.*
168. *Id.*
169. *Id.*

Table 1 to Paragraph (f)

Payment or benefit	Limitation per person or legal entity ($)
(1) Price Loss Coverage, Agriculture Risk Coverage payments (other than Peanuts)	125,000 per program year.
(2) Price Loss Coverage and Agriculture Risk Coverage payments for Peanuts	125,000 per program year.
(3) CRP annual rental payments	50,000 per program year.
(4) NAP payments	
(i) basic 50/55 NAP coverage	125,000 per crop year.
(ii) Buy-up NAP coverage	300,000 per crop year.
(5) LFP	125,000 per program year.
(6) CSP[1]	200,000.
(7) EQIP[2]	450,000.
(8) AMA program	50,000 per fiscal year.
(9) ECP	500,000 per disaster event.
(10) EFRP	500,000 per disaster event.

[170]

b. Individual Person Limitations

An individual person may qualify for only one total payment limit per program per year.[171] This includes payments made directly to the person and payments made to the individual through an entity in which the person has a direct or indirect ownership interest.[172] As previously discussed, the process of tracking payments through various levels of entity ownership to an individual person is

170. *Id.*
171. *Id.*
172. 7 C.F.R. § 1400.105(a) (2023).

known as direct attribution.[173] Thus, for a person who qualifies individually for a payment under a particular program, but also owns an interest in a legal entity that qualifies for a payment under the same program, the USDA will combine the payment amounts up to the relevant payment limit.[174] Current regulations require direct attribution through four levels of ownership in multi-person legal entities as discussed.[175]

III. The (Perhaps) Unintended Consequences Of Restricting Limited Liability Entities To One Payment Limit

Since the introduction of payment limits under the 1938 Farm Bill, arguments have raged both for and against them and their method of enforcement. After 2008, those arguments have included that the definition of person restricts limited liability entities, such as corporations and LLCs, to a single payment limit.[176] Proponents of this change hail it as a measure preventing the use of elaborate entity structures to circumvent payment limits.[177] However, one can level several criticisms against the treatment of limited liability entities under this rule. In fact, many of these criticisms directly confront the stated goals of current farm policy.[178]

A. A Distinction Without a Difference

"That's a distinction without a difference!" Law students likely learn this invective on the first day of class, whether leveled at their arguments by the professor or used by the student to attack the rule in a case. The phrase decries disparate treatment of entities or principles that are functionally and practically indistinguishable. In the instant discussion, one can argue that treating corporations or LLCs, and particularly pass-through entities such as S corporations and pass-through LLCs, differently from partnerships amounts to a distinction without a difference.[179]

173. *Id.* § 1400.105(d).

174. *Id.*

175. *Id.* § 1400.105(c)(1)–(4).

176. JIM MONKE, CONG. RSCH. SERV., RL34594, FARM COMMODITY PROGRAMS IN THE 2008 FARM BILL 14 (2008), https://www.everycrsreport.com/files/20080930_RL34594_3d75a073c58af62b5b67f67d32a6341776eac5a8.pdf [https://perma.cc/C38P-Z3NJ].

177. *Id.* at 17.

178. *See id.* at 1–2.

179. *See generally* 7 C.F.R. § 1400.105 (2023).

Clearly, the limited liability nature of such entities is a key difference, though perhaps a difference of far less magnitude than proponents of the current approach claim. Putting the treatment of liability issues aside, however, one could argue partnerships and limited liability entities share more similarities than differences.

Consider the fact that many businesses choosing the pass-through LLC as their entity form do so precisely because it almost exactly replicates the partnership business form.[180] The operating agreement may almost mirror a partnership agreement: decision-making functions as it would in a partnership, there is often a single class of membership, allocations of gain, loss, revenue, and expense are allocated just as they would be in a partnership, and taxation is handled exactly as it would be in a partnership. Indeed, the only distinction between an LLC and a partnership, in these cases, are the organization process and the limited liability feature.[181] These businesses clearly want to function in almost all material ways like a partnership and, perhaps most importantly to some policy makers, want to be taxed like a partnership.

Many business and tax practitioners would argue the pass-through LLC is the limited liability entity form most closely resembling a partnership, with the S corporation being a close second. The principal distinction between a partnership and an S corporation lies in the formalities and management restrictions imposed on the S corporation: limit of 100 shareholders, all shareholders must have common stock, and all shareholders must be United States citizens or residents.[182] As such, one could argue that the added restrictions needed for S corporation status make it an even better candidate for managing potential payment limit abuse than a partnership. Further, just as with an LLC, S corporation tax treatment is functionally quite similar to that of a partnership.[183]

Viewed through a functional analysis lens, the entity formations most closely resembling a partnership are pass-through LLCs, separately taxed LLCs, and S corporations. Perhaps furthest from the partnership form is the C corporation, both in terms of taxation and functional structure. That said, C corporation organizers have significant freedom to structure their bylaws to make the function of the corporation closely follow that of the partnership form, albeit within the

180. WILLIAM K. SJOSTROM, JR., BUSINESS ORGANIZATIONS: A TRANSACTIONAL APPROACH 18–19 (4th ed. 2023).

181. Jason Fernando, *What is an LLC? Limited Liability Company Structure and Benefits Defined*, INVESTOPEDIA (Sept. 30, 2023), https://www.investopedia.com/terms/l/llc.asp#:~:text=The%20primary%20difference%20between%20a,the%20LLC’s%20debts%20and%20liabilities [https://perma.cc/N8SA-ZPXD].

182. 26 U.S.C. § 1361(b)(1)(A)–(D).

183. *See generally id.* § 1366.

framework of C corporation requirements under the Internal Revenue Code and state laws.[184] Clearly, C corporation taxation lies on the far end of the continuum from partnership taxation, so if taxation approach represents the compelling rationale for different treatment of limited liability entities under the payment limitation rules, the point is fair. However, if the rationale is functional form, one can imagine any number of ways the C corporation could be made to conform to the functional requirements deemed important by policymakers. Admittedly, C corporations have seen reduced use in agriculture, particularly as land-owning entities, since the changes made to taxation of capital gains and the treatment of capital asset acquisition and disposition transactions under the Tax Reform Act of 1986.[185] That said, C corporations formed to carry out farm operations primarily bear the weight of Farm Bill payment limitations, not those formed to hold land.[186]

Since the legislative history is unclear as to why the Farm Bills have treated limited liability entities differently than sole proprietorships, general partnerships, and joint ventures, one must speculate as to the reasons why. If Congress viewed limited liability entities as simply functioning differently than general partnerships, that seems a misapprehension. As discussed, almost all limited liability entities can function like a partnership with proper design.[187] If Congress was swayed by the specter of the "evil corporate farm" and thus chose not to treat limited liability entities like other business forms, it should consider that the most recent Census of Agriculture reports nearly 90 percent of incorporated farm operations, which under the USDA's definition includes LLCs, are family-held.[188] Whatever the case, asserting a functional difference between limited liability entities, limited to one payment limit, and partnerships, allowed the sum total payment limits of their members, as the basis for their disparate treatment under the payment limitation rules does not pass muster.[189]

B. Limited Liability ≠ "No Risk" and Farms are Forced to Choose Entity

184. *See generally Bylaws, Stock Options and Other Requirements for C Corporations*, FUSION CPA (Dec. 13, 2022), https://www.fusiontaxes.com/thought-leadership/blog/bylaws-stock-options-and-other-requirements-for-c-corporations/ [https://perma.cc/3JM3-FMZK].

185. *See* Tax Reform Act of 1986, Pub. L. No. 99-514, §§ 301–311, 100 Stat. 2085, 2216–20.

186. *See* Roger A. McEowen, *Farm Service Agency Adjusted Gross Income Calculation Could Influence Choice of Entity*, IOWA STATE UNIV. CTR. FOR AGRIC. L. AND TAX'N (April 18, 2014), https://www.calt.iastate.edu/article/farm-service-agency-adjusted-gross-income-calculation-could-influence-choice-entity [https://perma.cc/R758-G69C].

187. *See supra* p. 36.

188. U.S. DEP'T OF AGRIC. NAT'L AGRIC. STAT. SERV., 2017 CENSUS OF AGRICULTURE 170 (2019).

189. PAYMENT ELIGIBILITY AND PAYMENT LIMITATIONS, *supra* note 57, at 3.

Structures with Unlimited Joint and Several Liability

"Because the company shields its owners from liability (or risk), the company is given a single payment limit regardless of the number of owners."[190] A 2020 Congressional Research Service report makes this observation in its explanation of why "[a] legally defined association of joint owners or shareholders is treated as a single person for purposes of determining eligibility and payment limits."[191] Again, given the lack of legislative history on the topic, it is difficult to say why Congress restricted limited liability entities to only one payment limit. If it was because they viewed a limited liability entity as an impenetrable shield against every form of risk to the farmer who used it and thus reducing or eliminating the need for any risk mitigation tools afforded by the Farm Bill, it was laboring under a massive misunderstanding of the concept of limited liability.[192]

1. The Limited Liability Feature of LLCs and Corporations Only Allows Farmers to Limit Their Risk Exposure to Their Investment in the Entity, and Only in Some Circumstances

First, one must consider the concept of the limited liability created by an entity such as a corporation or LLC.[193] Limited liability entities function as artificial persons in that they have many of the same legal rights and obligations as natural persons.[194] Entities can: receive, hold, and dispose of property; engage in most transactions as a natural person would; and can sue and be sued.[195] This last point is critical to the instant discussion. Corporations and LLCs face almost every form of liability confronted by a natural person, from tort liability to loan foreclosures.[196] The only difference is that while all the assets of the entity, including the equity of the owners, are at risk to satisfy those liabilities, the personal assets of the owners held outside the entity are not.[197] Therein lies the only real "limitation" on liability for the owners of the corporation or LLC. The

190. STUBBS & ROSCH., *supra* note 27, at 5.

191. *Id.* Interestingly, two sentences later the same report observes "[n]early 90% of incorporated farm operations are family held."

192. Priyanka Prakash, *Partnership vs. Corporation: Key Differences and How to Choose*, NERDWALLET (May 11, 2022, 11:28 AM), https://www.nerdwallet.com/article/small-business/partnership-vs-corporation-key-differences-and-how-to-choose. [https://perma.cc/DZZ7-JLPZ].

193. Attorneys and law students who stayed awake in their Business Organizations class may wish to skip ahead.

194. 18 AM. JUR. 2D *Corporations* § 65 (2023).

195. *See, e.g.*, 18 AM. JUR. 2D *Corporations* § 1809 (2023).

196. 18B AM. JUR. 2d *Corporations* §§ 1785, 1811 (2023).

197. *See* 18 AM. JUR. 2d *Corporations* § 46 (2023).

impact of this limitation on the farmers who own the entity is entirely dependent on the amount of their investment.[198] If they have placed a significant amount of their personal wealth into the entity, all of that wealth is at risk for the liabilities of the entity.[199] Put another way, the control a limited liability gives over risk is limited to the amount a farmer invested into the farming entity.

One should also note that even this limitation is not an immutable one. For example, lenders to a farming corporation or LLC will frequently require personal guarantees of the entity's debts by the owners.[200] Therefore, in some circumstances, even the limited liability entity cannot protect the personal assets of the owners.[201] If policymakers worry about limited liability entities being used to shield their owners from liability for malfeasance under the Farm Bill programs, they should remember there are numerous remedies under both criminal and civil laws for such actions that can place personal liability on the entity owners.[202]

2. Limited liability Entities Face Every kind of Risk Sole Proprietorships and Partnerships Do

The USDA recognizes five general types of risks faced by farms:

> *Production risk* derives from the uncertain natural growth processes of crops and livestock. Weather, disease, pests, and other factors affect both the quantity and quality of commodities produced.
>
> *Price or market risk* refers to uncertainty about the prices producers will receive for commodities or the prices they must pay for inputs. The nature of price risk varies significantly from commodity to commodity.
>
> *Financial risk* results when the farm business borrows money and creates an obligation to repay debt. Rising interest rates, the prospect of loans being called by lenders, and restricted credit availability are also aspects of financial risk.

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198. Jesse J. Richardson, Jr. & L. Leon Geyer, *Ten Limitations to Ponder on Farm Limited Liability Companies*, 4 DRAKE J. OF AGRIC. L. 197, 198 (1999).

199. *Id.*

200. *Id.* at 199.

201. *Id.*

202. *See* Chad G. Marzen, *Crop Insurance Fraud and Misrepresentations: Contemporary Issues and Possible Remedies*, 37 WM. & MARY ENV'T L. & POL'Y REV. 675, 684–707 (2013); *see also* CHARLES DOYLE, CONG. RSCH. SERV., R43293, CORPORATE CRIMINAL LIABILITY: AN OVERVIEW OF FEDERAL LAW 4–7 (2013).

> *Institutional risk* results from uncertainties surrounding Government actions. Tax laws, regulations for chemical use, rules for animal waste disposal, and the level of price or income support payments are examples of government decisions that can have a major impact on the farm business.
>
> *Human or personal risk* refers to factors such as problems with human health or personal relationships that can affect the farm business. Accidents, illness, death, and divorce are examples of personal crises that can threaten a farm business.[203]

The authors bring these risk areas to the attention of the reader for one reason: every single one of these risk categories is faced squarely by every farming operation, regardless of their ownership form. Indeed, Farm Bill programs were formed precisely to help farmers deal with these risks, particularly production and price risk.[204] The operation of the farm through an LLC or corporation does nothing to eliminate those risks; the only limitation to the liability of the entity's members is the amount of their personal wealth they have invested in the entity.[205] Conversely, limiting a corporation or LLC to one payment regardless of the number of actively engaged participants in the entity severely curtails the availability and potency of the risk management tools a farm can access.[206]

3. Functionally Forcing Farmers to Use the Sole Proprietorship and Partnership Forms Forces Them to Assume Even Greater Risks

Discouraging farmers from using limited liability business entity forms functionally encourages them to use sole proprietorship or partnership forms. Any liability and risk protections that derive from the limited liability entity forms are completely absent from the sole proprietorship or partnership forms.[207] Much to

203. *Risk in Agriculture*, U.S. DEP'T OF AGRIC. ECON. RSCH. SERV. (May 3, 2023), https://www.ers.usda.gov/topics/farm-practices-management/risk-management/risk-in-agriculture/#:~:text=Five%20general%20types%20of%20risk,and%20human%20or%20personal%20risk [https://perma.cc/52PZ-6V27].

204. *See generally* Francis Tsiboe & Dylan Turner, *Government Programs & Risk*, U.S. DEP'T OF AGRIC. ECON. RSCH. SERV. (May 3, 2023), https://www.ers.usda.gov/topics/farm-practices-management/risk-management/government-programs-risk/ [https://perma.cc/VQ8E-LPRY].

205. Mike Downey, *Does Your Farm Need an LLC?*, FARM PROGRESS: FARM FUTURES (July 19, 2022), https://www.farmprogress.com/commentary/does-your-farm-need-an-llc- [https://perma.cc/U5D5-URQ6].

206. *See generally* Tsiboe & Turner, *supra* note 205.

207. Nellie Akalp, *Is a Farm LLC Really Necessary?*, CORPNET (Dec. 21, 2022), https://www.corpnet.com/blog/farm-

the contrary, those forms carry unlimited liability, and in the case of the joint partnership, carry unlimited joint and several liability.[208] One does not need to go to law school to imagine that a sole proprietor has no protections at all from any form of liability. All of a sole proprietor's assets are at risk for any of their acts or omissions, but the concept of joint and several liability may not be as apparent.

The Uniform Partnership Act states plainly that "all partners are liable jointly and severally for all debts, obligations, and other liabilities of the partnership unless otherwise agreed by the claimant or provided by law."[209] Perhaps the most succinct summary of joint and several liability comes from Black's Law Dictionary:

> Liability that may be apportioned either among two or more parties or to only one or a few select members of the group, at the adversary's discretion. Thus, each liable party is individually responsible for the entire obligation, but a paying party may have a right of contribution and indemnity from nonpaying parties.[210]

This means if the farming partnership incurs a liability of some form, *all* of the partners bear responsibility. If one of the partners skips town and cannot be found, the remaining partners are on the hook with only a right of contribution against the missing partner for their fair share of the liability.[211] Further, a partner in a general partnership is liable for their own acts or omissions in addition to those of their partners so long as their acts were within the scope of the partnership's business.[212] As a result, the acts of a single partner can incur liability for all the partners.

As distinguished from a limited liability entity, in a general partnership, a partner's individual liability for the liabilities of the partnership is not limited to their investment therein.[213] Although partnership law generally directs the assets of the partnership itself be consumed first to satisfy its liabilities, if those assets

llc/#:~:text=Unlike%20a%20Sole%20Proprietorship%20or,legal%20responsibilities%20are%20its%20own [https://perma.cc/372M-MP2Y].

208. Andrew Bloomenthal, *General Partnerships: Definition, Features, and Example*, INVESTOPEDIA (Aug. 14, 2023), https://www.investopedia.com/terms/g/generalpartnership.asp#:~:text=Partners%20in%20a%20general%20partnership,of%20any%20and%20all%20employees [https://perma.cc/LYB2-2898].

209. UNIF. P'SHIP ACT § 306(a) (UNIF. L. COMM'N 2013).

210. *Joint and Several Liability*, BLACK'S LAW DICTIONARY (7th ed. 1999).

211. Bloomenthal, *supra* note 208.

212. UNIF. P'SHIP ACT § 306(a) (UNIF. L. COMM'N 2013).

213. Bloomenthal, *supra* note 208.

are insufficient, the assets of the partners themselves can be claimed.[214] Thus, the acts or omissions of a partner can trigger not only the loss of all the assets contributed to the partnership, but also the loss of the partners' individual assets. This means the partnership form can sometimes amplify legal risk for the partners compared to the limited liability entity forms.

4. Farmers Can Use the Partnership Form and Take Advantage of Limited Liability, but only with Significant Additional Cost and Complexity

Imagine for a moment: three individuals want to start a business with production, price, financial, institutional, and human risk factors unlike those faced by any other industry. These three individuals go to an attorney for help organizing the business. Assessing these formidable risk factors, the attorney strongly suggests an LLC or corporation to limit the individuals' risk to their investment in the business. "Not so fast, buddy," one of them says, "using an LLC or corporation limits us to the payment limit of only a single person for some of the most important risk management tools in our industry. If we were a partnership, we could get the benefit limits of *all* of us combined." Bewildered, the attorney explains the joint and several liability risks of that partnership form. "Well," says another member of the group, "isn't there some way to have our cake and eat it too? Can't we come up with a structure that lets us combine our payment limits?" The attorney says, "Let me think about it." After days of headache-inducing review of the "short reference" on Farm Bill payment limitations (said short reference weighing in at 558 pages), the attorney stares at their markerboard with so many scribblings and lines as to make an observer think they were a conspiracy theorist. Finally, a eureka moment occurs. It can be done if there is a partnership *of* limited liability entities.

She calls her clients back into the office and shows them the diagram in Appendix A.[215] Each of the individuals will form a single-member LLC and contribute the assets the individual would have contributed to the partnership. In turn, those LLCs will become the partners of the partnership and contribute their assets to the partnership. The partnership will operate the business and report its income, expenses, gains, and losses to the LLCs via a Schedule K-1 prepared for

214. 68 C.J.S. *Partnership* § 216 (2023). ("Under the equitable doctrine of 'marshalling of assets,' partnership assets are applied first to the discharge of the partnership liability; thus, a partnership creditor cannot reach the partners' personal assets unless the partnership assets are first exhausted or there is no effective remedy without resort to the individual partners' property.").

215. *See infra* Appendix A.

each of the LLCs after the partnership return is completed.[216] The LLCs, in turn, report those items to their individual owners on their Schedule K-1s prepared after the LLC returns are prepared.[217] Now, the partnership functionally can combine the payment limits of the LLCs, which are each limited to one payment limit (presumably acceptable to their respective individual person owners), with no loss of payment eligibility.[218] All it took was the formation of four entities, a partnership and three LLCs. This requires the preparation of a partnership agreement, three LLC operating agreements, state filing documents for each entity, the annual preparation of one partnership return, four LLC returns, and six Schedule K-1s. However, if LLCs were able to combine the payment limitations of their members, the same level of protection could have been accomplished with one LLC operating agreement, one state filing, one LLC return, and three Schedule K-1s.

If a client in any other business went to their attorney to discuss business formation in a high-risk industry, any attorney worth their salt would recommend a limited liability form. Yet, the Farm Bill, ostensibly created for the sole purpose of managing the extraordinary risks in production agriculture, functionally takes those entity forms off the table in jeopardy of being affected by the payment limits. The only way to attempt some mitigation of those risks is to create an entity structure such as the one above. Making the Farm Bill payment limitations entity agnostic would eliminate such a need. In this regard, the Farm Bill's treatment of payment limits for limited liability entities is not only a distinction without a difference, but it seems to add insult to injury or, at the very least, complexity and cost to risk.

C. Farms Lose Access to Entity Forms with Several Advantages in the Farm Transition Process

This discussion now comes to the heart of the matter. Beyond the notion that the Farm Bill's distinction between partnerships and limited liability entities constitutes a distinction without a difference, limiting LLCs and corporations to one payment also functionally takes away a powerful risk-management tool from farmers and ranchers. One must confront the fact that the current rules make successfully transitioning the family farm to the next generation more difficult.

216. *See* Troy Segal, *Schedule K-1: Partner's Share of Income, Deductions, Credits, Etc.*, INVESTOPEDIA (Apr. 30, 2023), https://www.investopedia.com/ask/answers/09/k-1-tax-form.asp [https://perma.cc/3U29-4ERN].

217. *Id.*

218. Assuming the individuals do not receive any Farm Bill payments through other entities.

The outcome of farm transitions will define the structure of United States agricultural production and many rural communities over the next 20 years. It is estimated that the Baby Boomer generation stands to inherit approximately $6.0 trillion in assets from their parents, but they will inherit it far later in life than any preceding generation.[219] With Baby Boomers currently between 59 and 78 years old, those $6.0 trillion in assets will likely transfer to Generation X and the Millennials within the next two decades based on average life expectancy in the United States.[220] This correlates with the USDA Census of Agriculture data which shows over a third of farm operators in the United States are 65 or older with one million farmers within ten years of that mark.[221]

The coming decades will almost certainly see an unprecedented turnover in the ownership and management of farms in the United States. But a turnover to whom? Will farm children come back to the farm to continue the family business? Will off-farm heirs rapidly rise as the predominant landowners? If so, will they hold or lease the land, and if they lease it, to whom? Or will institutional investors grow in prominence as agricultural landowners? Everyone from farmers to residents of rural areas and the businesses who serve them have a vested interest in the answers to these questions. With so many unknowns surrounding generational transitions, farm policy in the United States should be doing everything in its power to make the transition easier—not harder. This especially applies to those wanting to participate in the operation and share in its risks.

Clearly, the successful transition of family farms carries wide-ranging implications. These transitions, however, are fraught with formidable challenges. A 2007 survey revealed that 55% of adults in the United States did not have a

219. Alicia H. Munnell et al., *How Important are Intergenerational Transfers for Baby Boomers?* 1 (Ctr. for Ret. Rsch. at Boston Coll., Working Paper No. 2011-1, 2011).

220. *See id.*

221. U.S. DEP'T OF AGRIC. NAT'L AGRIC. STAT. SERV., 2017 CENSUS OF AGRICULTURE HIGHLIGHTS – FARM PRODUCERS 2 (2019), https://www.nass.usda.gov/Publications/Highlights/2019/2017Census_Farm_Producers.pdf [https://perma.cc/3H4K-QHRE]; Chuck Abbot, *On Average, U.S. Farmers Are Aging, but a Quarter of Them Are Newcomers*, FERN'S AG INSIDER (Apr. 11, 2019), https://thefern.org/ag_insider/on-average-u-s-farmers-are-aging-but-a-quarter-of-them-are-newcomers/#:~:text=Environment%20Reporting%20Network-,On%20average%2C%20U.S.%20farmers%20are%20aging%2C%20but%20a,quarter%20of%20them%20are%20newcomers&text=One%2Dthird%20of%20America's%203.4,according%20to%20new%20USDA%20data [https://perma.cc/Y2YU-BEYF] (commenting on the rising average age of farmers).

will.[222] One might think the asset intensity of farming would encourage farmers to be more proactive in the disposition of their assets given that the average net worth of a farm in the United States is estimated to be approximately $1.57 million.[223] Estate planning research focused on the agricultural sector suggests the number of farmers with any manner of estate planning in place to be far worse, with estimates hovering at a mere 36%.[224] In his review of the literature on farm transitions, financial planner Kevin Spafford points to the lack of estate planning as one of three primary points of failure in the farm transition process: (1) inadequate estate planning; (2) insufficient capitalization or poor financial performance of the farm enterprise, rendering it vulnerable to the financial stresses inherent in a transition; and (3) a failure in adequately preparing the next generation for their management and asset ownership roles following the transition.[225]

What does all this have to do with the disparate treatment of limited liability entities under the current Farm Bill payment limitations? The answer lies in the tremendous flexibility limited liability entities have to address all three areas of concern while also providing the critical risk management component discussed in the preceding section.

1. Entities as an Estate Planning Tool

Much speculation exists as to the cause of the phenomenally high rate of farmers without any business succession planning. The reasons most likely include a reluctance, or phobia, of farmers to confront their mortality and avoid emotional conversations. A survey of over 600 Texas farmers and ranchers found that nearly 30% of the responses could be categorized as either a fear of family conflicts or simply not knowing where to start.[226] Nevertheless, the old adage "failing to plan

222. *Majority of American Adults Remain Without Wills, New Lawyers.comSM Survey Finds*, LEXISNEXIS (Apr. 3, 2007), https://www.lexisnexis.com/community/pressroom/b/news/posts/majority-of-american-adults-remain-without-wills-new-lawyers-comsm-survey-finds [https://perma.cc/26D6-KCEQ].

223. *Tailored Reports: Farm Business Balance Sheet*, U.S. DEP'T OF AGRIC. ECON. RSCH. SERV. (Dec. 15, 2022), https://my.data.ers.usda.gov/arms/tailored-reports [https://perma.cc/P63J-T7PG] (see "Farm equity" for 2021 in either chart).

224. KEVIN SPAFFORD, LEGACY BY DESIGN: SUCCESSION PLANNING FOR AGRIBUSINESS OWNERS 6 (2006).

225. *See id.* at XI.

226. TIFFANY DOWELL LASHMET & JUSTIN BENAVIDEZ, SURVEY OF TEXAS AGRICULTURAL PRODUCERS AND LANDOWNERS 20 (2022), https://agrilife.org/texasaglaw/files/2023/02/Survey-of-Texas-Agricultural-Producers-and-Land-Owners.pdf [https://perma.cc/V2B4-J8TL]. Of the 604 survey responses, only 161 even answered the question, which was "If you do not have a succession plan in place, what is the

is planning to fail" holds true. In the authors' experience, when one asks a farmer what they want to happen after they die, the answer invariably resembles something along the lines of "I want to keep the farm together and I want to keep the family farming." Thus, confronting farmers with the fact that failing to have some plan in place likely means the fulfillment of their greatest fear, the disuniting of both family and farm, often represents the best hope of getting their transition process in motion.

Rather than playing to these fears, a transition process can instead give farmers a positive view of what the future may look like. Considering the formation of an LLC or corporation as a succession plan for the farm business and how to organize the business to align with the values of stakeholders provides a starting point for organization of the business and for an "awakening" in the mind of the farmer that estate planning can be hopeful rather than depressing.[227] Therefore, discussions about the entity formation, structure, and operation have value not only during formation, but they can also remind the farmer of their primary objective—ensuring the farm and the family survive by enhancing the survivability of the business.[228] Entity formation serves a key role in "jump-starting" the transition process itself. Once the farmer realizes the importance of transition planning to the farm's continued success, they may be more likely to engage on all points of the process.

2. Entities as a Tool to Deal with Financial Stressors During a Generational Transition

It is almost axiomatic that significant disruptive events increase the probability of failure for a business already under financial stress. Everything from the Dust Bowl, to the Farm Crisis, to the COVID-19 pandemic demonstrate this concept. The same holds true for the death of the principal operator of a farm. A farm in anything less than top financial condition, and even some farms that are in such condition, face a number of financial stressors posing an existential threat to the farm as it attempts to navigate the generational transition.[229]

biggest roadblock keeping you from doing so?" Though it leaves much to interpretation, the lack of responses to the question is perhaps telling in and of itself.

227. *See* SHANNON L. FERRELL ET AL., OKLA. STATE UNIV. EXTENSION, FARM TRANSITIONS i-10 (Oct. 2, 2023, 4:34 PM), https://extension.okstate.edu/programs/farm-transitions/first-steps/site-files/introduction-the-importance-of-farm-transition-planning.pdf [https://perma.cc/BR2R-RFKV].

228. *Id.*

229. Raney Rapp, *Succession: Transitioning Farms to the Next Generation Successfully a Daunting, Difficult Task*, FARM TALK (Dec. 27, 2022),

a. Facilitating Business Information Access

First, the farm may be performing poorly but the surviving farm stakeholders had no idea since the principal operator worked in a "black box."[230] That is, the principal operator followed a "command and control" management style with a perception… that strong leadership moves people and organizations forward, so the command and control organizational system is a perfectly acceptable way to run the business, and subordinates should accept decisions made by the leaders, sometimes without question or any need of leadership to explain how or why things are done the way they are.[231] In other words, the principal operator felt the financial condition of the operation was no one's business but their own, and thus no one else had access to the farm's financial records to the extent needed to genuinely understand its true state.[232] All management information and decisions were kept in the black box and the principal operator only allowed themself to see inside it.[233]

A properly constructed entity can obviate this problem. Engaging all the farm stakeholders in deciding how the entity will operate requires creation of communication channels and rules for how the farm's financial decisions are to be made and communicated to the owners.[234] Moreover, entities such as LLCs and corporations benefit from protections to members and shareholders guaranteeing their access to information about the state of the entity.[235]

b. Facilitating Farmer Retirement (Whatever that is …)

Second, farmers often fail to realize they may need to decrease their financial dependence on the farm to facilitate the entry of the next generation and its concomitant increase in that generation's dependence on the farm. To paraphrase, "[they] must increase, but I *must* decrease."[236] Farmers notoriously resist the

https://www.farmtalknews.com/news/transitioning-farms-to-the-next-generation-successfully-a-daunting-difficult-task/article_4d8b2056-863b-11ed-aa10-17a996eaf2d8.html [https://perma.cc/RK3P-SBZ5].

230. FERRELL ET AL., *supra* note 227, at i-9.

231. *Id.* at 2-6 to 2-7, *citing* W. Strauss and N. Howe (1991). GENERATIONS.

232. *Id.*

233. *See id.*

234. DEL. CODE ANN. tit. 8, § 220 (2023).

235. *See, e.g.*, UNIF. LTD. LIAB. CO. ACT § 410 (UNIF. L. COMM'N 2006).

236. *See John* 3:30 (King James).

concept of retirement. Surveys in Wisconsin indicate that 73% of farmers plan either to never retire or to only "semi-retire."[237]

While the link between farmers' retirement attitudes and farm financial stress in a transition may not be apparent, failing to adequately prepare for retirement expenses can have devastating consequences for the survivability of the farm.[238] One predominant issue for older farm families is the rising cost of medical care.[239] By one estimate, a 65-year-old will need $157,000 in liquid funds to cover their medical expenses to the end of life.[240] Does the farm have enough liquid assets to cover expenses such as these? On average 80% of the value of a United States farm's assets are from land, with only 7% coming from other assets.[241] A failure to plan for these and other expenses—expenses that are commonly dealt with by a retirement plan—that come as the economic value of the farmer's contributions to the farm may be decreasing means greater financial stress for all stakeholders.[242]

Unsurprisingly, age does take a toll on the economic productivity of farmers. Farmers often decrease production or switch to less demanding enterprises as they age.[243] The average value of sales per farm for producers over 65 years of age is 42% lower than that of farmers 45 to 64 years old, despite the fact their farm size is only 7% smaller than the next-youngest cohort.[244] "The consequence of this 'retirement in place' by decreasing productivity of the farm assets can mean the conversion of hard-earned farm equity into living expenses for the current

237. Joy Kirkpatrick, *Retired Farmer – An Elusive Concept*, CHOICES, 2nd Quarter 2013, at 1, 1, https://www.choicesmagazine.org/choices-magazine/theme-articles/transitions-in-agriculture/retired-farmer—an-elusive-concept [https://perma.cc/G7CY-6PV3].

238. *Id.*

239. *See Trends in Health Care Spending*, AM. MED. ASS'N (Mar. 20, 2023), https://www.ama-assn.org/about/research/trends-health-care-spending [https://perma.cc/ZK97-HCHE].

240. Deanna Spaulding, *Fidelity Releases 2023 Retiree Health Care Cost Estimate*, FIDELITY NEWSROOM (June 21, 2023), https://newsroom.fidelity.com/pressreleases/fidelity—releases-2023-retiree-health-care-cost-estimate—for-the-first-time-in-nearly-a-decade—re/s/b826bf3a-29dc-477c-ad65-3ede88606d1c [https://perma.cc/H8NJ-VNW2].

241. *Tailored Reports: Farm Business Balance Sheet*, *supra* note 224.

242. *See* Kathleen Lonergan Erickson, *Stop Delaying Farm Succession Planning: Some Steps to Make Progress*, SUMMIT (Mar. 3, 2021), https://www.summitepc.com/blog/farm-succession-planning [https://perma.cc/4263-KDJB].

243. Loren W. Tauer, *Farmer Productivity by Age over Eight U.S. Census Years* 1 (Dyson Sch. of Applied Econ. & Mgmt., Cornell Univ. Working Paper No. 2017-08, 2017), https://dyson.cornell.edu/wp-content/uploads/sites/5/2019/02/Cornell-Dyson-wp1708.pdf [https://perma.cc/9K69-JMJT].

244. Derrell Peel, Damona Doye, and Mary Ahearn, *Drivers of Agricultural Transition*, CHOICES, 28(2) (2013).

generation occupying the farm."[245] While this may have been intentional all along, "it can also mean an undercapitalized business remains for the next generation."[246] Kirkpatrick summarizes the broader impacts of this "retirement effect:"

> Operators often slowly disengage from farming by eliminating livestock to reduce labor requirements but continue the cropping enterprises. Eventually, the farmer may opt to let the livestock facilities deteriorate, rent out the cropland, and continue living in the farmhouse in hopes the land will eventually transfer to his or her heirs at his or her death, in spite of the fact the heirs will never farm the land themselves . . . . This process may severely impact the older generation's retirement income potential, considering that farm business investments may be the only retirement assets. The only way to realize the older generation's return on investment is to continue farming or sell the farm outside the family at a fair market value, either as a working farm, recreational land, or for development. The other concern with timely identification of a successor is the infusion of Social Security income when the older generation reaches an age to receive benefits. The monthly income from Social Security and the addition of health care benefits through Medicare can provide just enough financial security to allow the older generation to be less reliant on a successful transition to the younger generation. Income from the Conservation Reserve Program can have a similar affect, but goes one step further by taking land completely out of production that might have otherwise been rented to a beginning farmer or a farmer expanding his or her operation.[247]

Frequently, this reduction in productivity occurs precisely as another family, that of the successor, is returning to the farm and understandably needs income for its support.[248]

> Summaries from two of the nation's largest farm-management databases suggest that, for operations supported primarily by on-farm income (as opposed to operations where the majority of income comes from off-farm employment), approximately $600,000 to $750,00 of gross sales are needed to support each full-time equivalent (FTE) worker on the farm. Based on an average asset turnover ratio of 30 percent, this level of sales requires approximately $2 million of assets under management. Many farms simply do not have this level of economic productivity or asset base.[249]

245. FERRELL ET AL., *supra* note 227, at i-6.
246. *Id.*
247. Kirkpatrick, *supra* 237, at 3.
248. *Id.*
249. FERRELL ET AL., *supra* note 227, at i-7.

"The problem becomes magnified when [one] consider[s] how many people may have to be supported by the farm asset base if another generation is added to the operation."[250] Adding a generation could warrant the inclusion of another full-time employee.[251] This could result in the cost-of-living withdrawals of two families encumbering the operation where there was only one before.[252] Further, "[t]he other problem posed by the addition of family members to the operation is that farm labor is, to borrow the economic terms, 'lumpy' rather than 'continuous.'"[253] This type of "lumpy" farm labor means that "instead of adding fractional amounts of [full time employees] to the operation, farmers generally can only add labor in integral units of one full-time employee at a time."[254] Correspondingly, significant increases in assets must be made to generate the cash flow needed to support the additional withdrawals—whether salary, living expenses, or both—of the additional employees.[255] "Without a long-term plan to grow the business and its assets, this can create significant problems, ranging from increased financial stress (particularly where debt is used to finance asset acquisition) to compensating added employees at below-market wage rates or a complete inability to add anyone to the operation."[256]

Taken together, these considerations shine a glaring light on the need for a clear plan allowing the senior generation to gradually step back from central roles in the operation and for the incoming generation to step in. An entity such as an LLC or corporation, provides the perfect vehicle to accomplish this purpose. Creating an LLC to house the farming operation could be coupled with an agreement that the incoming generation will buy a specific percentage of the entity over time—for example, 5% each year for 25 years. This creates a host of advantageous features for both generations: (1) the senior generation can harvest some of the equity they have built in the operation and can use that cash to manage their expenses and/or to invest to provide cash flows independent of the farm; (2) the schedule of purchases can be structured to both gradually decrease income distributions to the senior generation and increase distributions to the incoming generation—both generations have time to adapt their cash flows and manage off-farm income sources; (3) the incoming generation does not need to purchase the farm operation all at once but rather can spread out the purchase over time; (4) individual assets do not have to be purchased in separate transactions; rather, asset

250. *Id.*
251. *Id.*
252. *Id.*
253. *Id.*
254. *Id.*
255. *Id.*
256. *Id.*

ownership remains with the business and asset purchases and sales (and their tax impacts) can be passed through to the members in proportion to their ownership; (5) there is no need to partition land or create divided titles and co-tenancies since land ownership can remain with the entity if needed; and (6) the sale and purchase of entity ownership and the accompanying voting rights can be managed to facilitate a gradual shift of ownership control.

This last point bears further examination since it may represent yet another reason why farmers might be reluctant to contemplate both retirement and transition planning. Formation of an entity as a tool for transitioning farm operations helps the farmer visualize their changing role with respect to the operation. As Captain Pete Mitchell observed when he contemplated the next phase of his career, "I'm a fighter pilot… It's not *what* I am, it's *who* I am."[257] Replace "fighter pilot" with "farmer" and one receives a keen insight into the mindset of farmers with respect to transitioning their operation. Particularly for multigenerational operators, farming and *being* a farmer lies at the core of one's very identity. "If I am not farming, then who am I?" The gradual shift of ownership creates an opportunity to show the senior operator they can still maintain a critical role in the farm business. Further, titles can matter. Consider a situation in which the senior operator is promoted from CEO, a title they may have had much of their adult life, to Chairman of the Board. They will still weigh in on critical matters and their experience and advice will still be utilized by the entity. This gives them clear, meaningful participation in the business that might not be possible with a simple outright sale of assets, and certainly not with an estate transfer.

c. Preventing Farm Breakups by Avoiding Intestacy Impacts

Can an entity really protect a farm against a senior operator's lack of estate planning? In short, the answer is maybe.

Recall that only 36% of farmers have any form of estate plan in place.[258] This means 64% of farms would fall into intestacy.[259] Another survey found 60% of Iowa farmers thought the "best" farm estate plan was to divide the farm among all the heirs equally.[260] These results are presented together because under the intestacy laws of most states, they bring about the same result: the inheritance of

257. TOP GUN: MAVERICK, (Paramount Pictures 2022).

258. SPAFFORD, *supra* note 224, at XI.

259. *Id.*

260. John R. Baker, Presentation at National Farm Business Management Conference: What's it Worth if You Stay on the Farm? (June 11, 2013) (available at https://agrisk.umn.edu/Conferences/Presentation/what_is_it_worth_if_you_stay_on_the_farm).

the farm in undivided interests by the remaining heirs.[261] Therefore, research shows that division may arise for a farm with modest financial performance and more than one heir.

Consider the model of a prototypical southern Great Plains wheat and cattle operation owned by a senior generation (father and mother) with two children—one returning to the farm to operate it and one off-farm heir with no intentions of actively engaging with the farm.[262] The model was calculated by using 20 years of net farm income data from the Kansas Farm Management Association as a proxy for variance in farm income, Reed *et.* al used a simulation to estimate the ability of the farm to pay for a number of farm transition strategies.[263] The first of these strategies was to give both the on-farm and off-farm heir equal undivided interests in the property, which functionally forced the on-farm heir to buy out the off-farm heir's interest if the on-farm heir wished to keep the operation as a going concern.[264]

Measured by the ability of the farm to avoid any of the model's failure criteria—including a farm debt-to-asset ratio exceeding 60% or a need for the farm to use its operating line of credit to service the debt incurred in buying out the non-farm heir—the "split it down the middle" strategy faile every time over hundreds of simulation runs.[265] The farm simply could not generate enough cash flow to afford the payments needed to buy out the interest of the off-farm heir, essentially forcing the breakup of the farm.[266] Simulations such as this one explain the frequent financial and emotional stresses faced by a farm when either the senior generation fails to enact an estate plan or decides that "[s]ometimes right isn't equal[,] [s]ometimes equal's not fair," regardless of the contributions made to the farm by the heirs.[267]

Given the extreme financial challenges of a farm heir being forced to buy out just one other heir (to say nothing of situations with multiple off-farm heirs), the success of a farm transition seems dependent on avoiding this circumstance. Enter

261. *See* FERRELL ET AL., *supra* note 227, at i-5–i-6.

262. Garret Reed et al., *A Model of Farm Transition Planning for the U.S. Plains*, 4 J. APPLIED FARM ECON. 59, 61 (2021), https://docs.lib.purdue.edu/cgi/viewcontent.cgi?article=1062&context=jafe [https://perma.cc/QWF5-3BQC].

263. *Id.* at 60.

264. *Id.* at 62.

265. *See id*. at 65–66.

266. *Id.*

267. *See id.*; CORB LUND, *S Lazy H*, on THINGS THAT CAN'T BE UNDONE (New West Records 2015).

the legal entity, once more. If the farming operation were held inside an LLC, for example, the LLC buy-sell provisions could provide the farm heir with the option to redeem the senior operator's ownership interest (even if in intestacy) on affordable terms based on the operation's historical financial performance. This could also avoid, or at least mitigate, the risk of the off-farm heir filing suit to partition the property and legally force the purchase of his or her interest by the on-farm heir or an outside party.

The authors wish to take a brief aside at this point. Why assume this transition strategy would force the on-farm heir to buy out the off-farm heir?[268] Though the authors lack empirical data on the frequency of scenarios wherein an on-farm heir is forced to purchase the interest of an off-farm heir, each author has abundant anecdotal evidence of this phenomenon, which bears out the predictions of microeconomic theory. Assuming both the on-farm heir and the off-farm heir are economically rational actors, they will seek to maximize their economic returns. Functionally, the off-farm heir has received a share of stock in the farm enterprise. However, since they do not intend to participate in the farm directly and receive returns, they have only two means of receiving an economic return from this inheritance. They can receive dividends (distributions of farm income), or they can sell the stock to harvest the value of its equity. The farm would be managed by the on-farm heir, who is also a "stockholder," but further receives returns to labor and management. In good times, the on-farm heir may wish to increase not only returns to equity, but also returns to labor and management. Thus, the on-farm heir would likely prefer reinvesting profits in the business (buy land, retire debt, upgrade equipment, etc.) rather than pay a dividend. In bad times, they would try to stop all non-essential payments, such as dividends. Thus, in good times or bad, the farm would not choose to pay dividends—an economically rational choice by the on-farm heir.

Where does this leave the off-farm heir? They might choose to hold their stock hoping for appreciation in its value which, depending on the measure and timeframe thereof, has historically been above 10%.[269] However, this is likely an

268. *See* Reed et al., *supra* note 262, at 62–63.

269. Artem Milinchuk, *The Growth of Farmland Investing*, FORBES (Sept. 16, 2022, 7:00 AM), https://www.forbes.com/sites/forbesfinancecouncil/2022/09/16/the-growth-of-farmland-investing/?sh=768c4061bd15 [https://perma.cc/X5CE-HCDP]. However, if one never intends to sell the land but rather simply hold it as rental property, that rate of return falls to approximately 3% percent. *See generally* Gary Schnitkey, "Cash Rent as a Percent of Farmland Price," *FarmDoc Daily* (6):211, November 8, 2016. Continued upward pressures on farm land values may lead this value to a range of 2-3% depending on the comparative rate of increase in cash rental prices. *See* David Denos, "What is a Better Investment? Purchase Farm Land and Rent it out or Finance the Purchase o Farmland?" LinkedIn, July 6, 2017.

impractical option given the objections of the on-farm heir who needs access to the land and the other agricultural assets received by the off-farm heir. Thus, the only practical choice is for the off-farm heir to sell their interest to the on-farm heir. The authors bring all this to the attention of the reader for three reasons . First, if the farm were placed in an entity such as an LLC or a corporation, the entity's governing documents could specify a policy for dividend payment, thereby providing an incentive for the off-farm heir to retain their investment. Second, a legal entity, or a group of legal entities, could provide numerous opportunities for both heirs to receive returns from the operation. This could be through a land-holding entity (of which both the on-farm and off-farm heirs could be owners or beneficiaries) and a farm operations entity. Third, the off-farm heir might be encouraged to place more capital at risk as an investment in the farm if they had access to better risk management tools. All of these factors weigh in favor of creating more options for entities to be used in the transition process and to avoid disincentivizing the use of entities in farm management.

3. Entities as a Tool to Prepare the Next Generation for Management and Ownership

Reed's findings connect strongly with Spafford's third reason for farm transition failures: a failure in preparing the next generation for their entry into management and ownership.[270] While Spafford spoke of this in terms of a lack of managerial experience for the incoming generation and a failure to transfer the experience of the senior generation, "failure to prepare the next generation" could also mean a failure to prepare the next generation for the stresses they will face in trying to buy out their off-farm heirs as illustrated by Reed.[271]

Contrast the findings of Reed with respect to the split it down the middle strategy with another strategy modeled: the "lifetime equity transfer."[272] Under this strategy, the operating assets of the farm were placed into an LLC, with the land placed into a trust where both the on-farm and off-farm heirs were made equal beneficiaries of income generated by the trust.[273] As mentioned above, the on-farm heir purchases the ownership interest of the senior generation over 20 years and the farm LLC then leases land from the land-holding trust for fair market value rent.[274] In stark contrast to the 0% success rate of the split it down the middle

270. *See* Reed et al., *supra* note 262, at 62–63; *see also* SPAFFORD, *supra* note 224, at XI.

271. *See generally* SPAFFORD, *supra* note 224, at XI; *See generally* Reed et al., *supra* note 262.

272. *See* Reed et al., *supra* note 262, at 62–63.

273. *See id.* at 63.

274. *See id.* at 64.

strategy, the exact same farm achieved a 99% success rate.[275] While this result underscores the power of legal entities to facilitate the economic success of a farm transition, this approach also carries the advantages of gradual transfers. Instead of an estate transfer which occurs suddenly at an unpredictable date, the legal entity approach intentionally creates an environment wherein both generations operate side-by-side.[276] This gradual approach allows opportunities for both generations to gradually grow into their new roles.

In turn, that feeds into Spafford's original hypothesis.[277] Successful farm transitions require not only the transfer of assets, but the transfer of experience.[278] Farming consists of a series of hard and often expensive lessons learned in operating a specific set of assets in an industry.[279] Much can be gained by creating an environment where a farmer and their successor operate side-by-side and the experienced operator slowly hands over the reins all the while making sure the incoming operator is ready to move into management.[280]

4. Entities as a Tool for Off-Farm Heirs to Become Involved in the Farm Operation

The discussion above described many of the challenges when one heir wants to operate to the farm but the other does not. What if the other heir *did* want to be involved with the farm in some way, even if that did not involve directly participating in the day-to-day operations? Could an off-farm accountant heir provide financial services? Could an off-farm lawyer heir provide contracting, leasing, and risk-management support? Could an off-farm market specialist work on direct-to-consumer sales? Could an off-farm heir simply see the farm as a good investment in which they want to participate but cannot do so directly due to the demands of their occupation? The list goes on and on.

While admittedly, some "farm kids" do not return to the farm because they do not have an interest in pursuing agriculture as a profession, many still have a deep connection to the farm and want to participate in some way. A legal entity may provide the path for these off-farm heirs to engage with the farm. By investing at-risk capital through the purchase of membership in the entity, these off-farm heirs would then be engaged with the farm and in a meaningful way and could

275. *See id.* at 65.
276. FERRELL ET AL., *supra* note 227, at i-9–i-10.
277. *See generally,* SPAFFORD, *supra* note 224.
278. *See id.* at 67.
279. *See generally* SPAFFORD, *supra* note 224.
280. *Id.* at 55.

helping it grow while also helping share risk among more individuals. A properly constructed entity and buy-in arrangement can align the economic interests of all the parties, further increasing the chances of a successful transition by reducing conflict and requiring all parties be actively engaged in those discussions for some time under this model. More opportunities for farm involvement might increase the odds that the off-farm heir returns to the farm and contribute to the economic activity of the nearby communities as "work from home" opportunities continue to grow.

D. Farmers Looking to Make Unrelated Beginning Farmers Their Successors Lose an Important Option in Facilitating that Process

The discussion to this point has focused on how legal entities can be used to facilitate the transfer of the farm business among family members. What about the fact that more and more farmers find themselves not facing the "farm kid/city kid" conundrum, but rather the "no farm kid at all" conundrum? The lack of farm-raised kids returning to the farm poses not only a farm transition problem, but a rural community problem.[281]

At the same time, many young people seek the opportunity to start farming for themselves, but the barriers to entry to agriculture can remain formidable.[282] One of the most difficult barriers is the asset-intensity of the industry and the cost of those assets.[283] In the most recent National Young Farmer Survey, 59% of all young farmers indicated finding affordable land to buy was "very or extremely challenging."[284] In an attempt to combat this issue, the USDA has launched numerous initiatives to attract new farmers to the industry.[285] Still, agriculture finds itself with exiting producers in search of a successor and young producers in search

281. *See* John Cromartie et al., *Why Some Return Home to Rural America and Why It Matters*, U.S. DEP'T OF AGRIC. ECON. RSCH. SERV. (July 6, 2015), https://www.ers.usda.gov/amber-waves/2015/july/why-some-return-home-to-rural-america-and-why-it-matters/#:~:text=The%20presence%20of%20family%20members,living%20in%20their%20home%20community [https://perma.cc/8PEJ-PY65].

282. SOPHIE ACKOFF ET AL., BUILDING A FUTURE WITH FARMERS 2022: RESULTS AND RECOMMENDATIONS FROM THE NATIONAL YOUNG FARMER SURVEY 70 (2022), https://www.youngfarmers.org/wp-content/uploads/2022/09/NationalSurveyReport22-1.pdf [https://perma.cc/2PFU-T6G8].

283. *Id.* at 44.

284. *Id.* at 8.

285. Sarah Campbell, *USDA's Support for Beginning Farmers and Ranchers*, U.S. DEP'T OF AGRIC.: FARMERS.GOV (Oct. 28, 2020), https://www.farmers.gov/blog/usdas-support-beginning-farmers-and-ranchers [https://perma.cc/X3LR-RYPX].

of a farm.[286] Many "matching" programs seek to form connections between these two groups.[287]

Yet again, legal entities have a role to play. While a parent and child have a lifetime to learn how each other works and their respective personal values, unrelated farmers and their newfound successors must start "dating" slowly and build both understanding and trust before getting "married" and forming a succession plan.[288] This may start with a share lease arrangement on some of the land owned by the senior farmer or hiring the successor to do custom work on the senior operator's farm.[289] If those arrangements go well, they may be scaled up to include more acres or activities. Eventually, the parties may feel a level of comfort with each other that permits them to commit to a transfer of the operation. Ideally, this arrangement is a win-win for both parties. The senior operator gets to harvest some of the equity they have built in the operation while the incoming operator gains access to an asset base and perhaps even the goodwill of the business for a lower price than he or she would have paid in assembling the assets and business him or- or herself.

A legal entity presents numerous advantages over other business forms. The limited liability feature of an LLC, for an example, provides protection to both parties in the event of a catastrophic loss in the business and, to an extent, malfeasance on the part of the other party.[290] Conversely, the unlimited joint and several liability of a general partnership would likely concern many potential succession pairs perhaps even to the point of dissuading them from the enterprise entirely.[291] The buy-sell agreement can provide both parties with an "off-ramp" if they later decide the arrangement has ceased to be beneficial for some reason.[292] There may be numerous tax advantages to the entity form depending on the

286. *Id.*; FERRELL ET AL., *supra* note 227, at i-4.

287. *Land Matching*, CTR. FOR RURAL AFFS. (Oct. 2, 2023, 7:35 AM), https://www.cfra.org/land-matching#:~:text=Farmer%20and%20rancher%20linking%20programs,legacy%20and%20promoting%20good%20stewardship [https://perma.cc/NJ4A-CXZL].

288. *See* ANNA ROSE PETERSEN & TAMARA CUSHING, TIES TO THE LAND: SUCCESSION PLANNING FOR RURAL LANDOWNERS 8 (2022), https://catalog.extension.oregonstate.edu/sites/catalog/files/project/pdf/pnw763.pdf [https://perma.cc/9GNB-2WDY].

289. *Id.* at 26.

290. Fernando, *supra* note 181.

291. PETERSEN & CUSHING, *supra* note 288, at 25.

292. *Id.* at 29.

structure and operation of the business.[293] As previously mentioned, the entity can significantly simplify the transfer of assets by allowing the parties to buy and sell membership units rather than individual assets such as pieces of equipment and parcels of land.[294] By the same token, the entity can also create a way of evening out, but not eliminating, the tax effects of those transfers.[295] Limited liability entities can create an arrangement that greatly increases the comfort of both the outgoing and incoming unrelated successors in a way that cannot be readily replicated with other business forms.

E. Can't You do all this with Partnerships Already? Kinda, but not Really

The experienced practitioner, or perhaps even the law student who has completed their Business Organizations class, may be saying to themselves, "LLCs and corporations are great, but couldn't you do almost all of this stuff with a partnership form too?" The answer is "yes, but—" with several big "buts" to be observed.[296] This Article addressed most of the advantages limited liability entities have over sole proprietorships and general partnerships but allows the authors to succinctly drive them home.

First, and perhaps foremost, comes the unlimited joint and several liability inherent in the partnership form.[297] However, to emphasize this point one more time, functionally requiring a farm business to use the sole proprietorship or partnership forms unnecessarily exposes the farm to legal or financial risks it could mitigate with a limited liability entity form. Various limited liability forms can also present significant tax advantages and flexibility than the partnership form, such as LLCs taxed as a corporation or C corporations,[298] LLCs electing for pass-through taxation, or almost exactly like a partnership in the case of an S corporation.[299]

293. *See* LAND GRANT UNIV. TAX EDUC. FOUND., AGRICULTURAL TAX INSTITUTE MANUAL 30 (2023) (giving an example of these advantages in the case of an S Corporation).

294. *See id.*

295. *See id.*

296. Sir Mix-A-Lot's ode to them notwithstanding, lawyers generally despise big buts.

297. *See* discussion *infra* Section III.B.

298. Changes made to the Internal Revenue Code in the 1986 Tax Reform Act and its treatment of capital gains generally dissuade agricultural landowners from placing real estate into a C corporation, but there may be several reasons the farming operations might be placed into a C corporation. *See generally* Tax Reform Act of 1986, Pub. L. No. 99-514, 100 Stat. 2085.

299. *See generally* 26 U.S.C. § 1366.

Second, the ability to change members with minimal disruption represents a core feature of the limited liability entity forms. A law student in Agency and Partnership will recall that changing a partner technically requires dissolution of the partnership and the formation of a new one if another partner joins.[300] Beyond additional flexibility in changing ownership, limited liability entities are better able to accommodate different classes of membership, which can provide far greater options for involving off-farm family members.[301]

Conversely, the best a partnership can do on that front is the limited partnership which, by the Farm Bill rules, would constitute a legal entity.[302] Further, the limited partner must be "seen and not heard," meaning they serve as passive investors with little or no management input or agency in the business unless the partnership agreement states otherwise.[303] Regardless of the definition of limited partnerships as legal entities, the authors have seldom, if ever, observed a limited partnership in agriculture where the limited partner properly understood and observed their limitations in that role.

Third, partnerships are creatures of the common law and earlier times.[304] The risk management and investment needs of modern businesses, particularly businesses as capital-intensive as agriculture, need tools like the modern corporation and LLC to match those challenges. Two friends with $5,000 who wanted to start a coffee kiosk at the local park would likely hear "Form an LLC!" from their attorney, especially after *Liebeck v. McDonald's*.[305] Yet the Farm Bill

300. *See* J. WILLIAM CALLISON & MAUREEN A. SULLIVAN, PARTNERSHIP LAW AND PRACTICE: GENERAL AND LIMITED PARTNERSHIPS § 16:4 (2022) ("At will partnerships continue only as long as no partner expresses a will to disassociate."); *see also* UNIF. P'SHIP ACT §801 (UNIF. L. COMM'N 1997) ("A partnership is dissolved, and its business must be wound up . . . in a partnership at will, the partnership's having notice from a partner, other than a [dissociated] partner" with express notice to withdraw from the partnership).

301. *LLC Membership Units: Everything You Need to Know*, UPCOUNSEL (May 5, 2022), https://www.upcounsel.com/llc-membership-units [https://perma.cc/GRK7-X2KF].

302. 7 U.S.C. § 1308(a)(3). *See generally* Paul Goeringer, *Farm Business: Family Limited Partnership as a Business Structure?*, AGFAX (Sept. 22, 2016), https://www.agfax.com/2016/09/22/farm-business-family-limited-partnership-as-a-business-structure/ [https://perma.cc/QDM2-DSEQ].

303. *See* UNIF. P'SHIP ACT §801; *see also* UNIF. LTD. P'SHIP ACT, §§ 302, 406 and comments to §406(a) (UNIF. L. COMM'N 2013).

304. Ladru Jensen, *Is a Partnership Under the Uniform Partnership Act an Aggregate or an Entity?*, 16 VAND. L. REV. 377, 377 (1963) http://scholarship.law.vanderbilt.edu/cgi/viewcontent.cgi?article=3820&context=vlr [https://perma.cc/Z4JX-5H85].

305. *See generally* Liebeck v. McDonald's Restaurants, P.T.S., Inc., No. CV-93-02419, 1995 WL 360309 (N.M. Dist. Aug. 18, 1994).

essentially says, "Sorry, it's just general partnerships for you. Unless you only want the risk tools that one of you could get." This is potentially problematic for a family of six active participants in a multi-million dollar business which requires 500 horsepower machines to be moved dozens of miles to reach hundreds of acres of farmland using semi-trucks on state highways.

Finally, could a farm have a successful transition under the current Farm Bill payment limitation rules using a partnership form and basic estate tools? Certainly, and many do. But farm policy should focus on doing everything it can to facilitate the successful transition of our family farms rather than adding constraints to that process, right? Suffice it to say then, in paraphrase of Annie Oakley, "Anything a partnership can do, an LLC or corporation can do better!"[306]

F. The USDA Has Used an Entity-agnostic Approach with Some Farm Programs in Very Recent Times

The USDA has shown a willingness and ability to use an entity-agnostic approach to farm programs. In administering payments made under the Coronavirus Food Assistance Program (CFAP), the USDA defined payment limits both for individuals and for "a corporation, limited liability company, limited partnership, trust, or estate."[307] The approach to payments to entities under the CFAP program shows just one way in which the USDA could adopt an entity-agnostic approach.

G. "BUT WHAT ABOUT SCOTTIE PIPPEN?!" Proper Application of Existing Rules Can Prevent Circumvention of Payment Limitations Even if Limited Liability Entities are Treated in the Same Manner as Partnerships and Joint Ventures

Would allowing LLCs and corporations to combine the payment limits of their members just like a partnership invite all kinds of nefarious business structures that would allow multimillionaire NBA players, like Scottie Pippen, to receive thousands of dollars in Farm Bill payments?[308] The policy discussed by this Article would allow a farm LLC formed by Elon Musk, Jeff Bezos, Bill Gates, and Tom Brady to amass millions in PLC payments. There exists a critical tool to

306. IRVING BERLIN, *Anything You Can Do (I Can Do Better)*, *in* ANNIE GET YOUR GUN (1946).

307. 7 C.F.R. §§ 9.7(e)(1), (e)(2)(i–iii) (2023).

308. *New Light Shed on Farm Subsidy Payments*, NBC NEWS (June 11, 2007, 2:35 PM), https://www.nbcnews.com/id/wbna19174311 [https://perma.cc/U73L-ARPX] (discussing how Pippen received $78,945 in conservation payments between 2003 and 2005 based on his ownership of agricultural land in Arkansas).

prevent such nefarious dealings: the current Farm Bill payment eligibility and limitation rules without legal entity restrictions.[309] The authors spent 4,419 words (roughly one-quarter of this Article's total length) "succinctly" explaining these rules, which was an attempt to encapsulate the FSA's nearly 600-page "short reference" on the subject.[310] One can certainly debate whether current Farm Bill payment limits are adequate for the current agricultural risk environment, whether the current payment eligibility rules are too byzantine or restrictive, and whether additional forms of eligibility should be available for off-farm family members who may not satisfy the AEF rules to encourage them to place at-risk investments in the farm—and the authors likely will at some later date. But within the narrow scope, the question "does allowing limited liability entities to combine payment limits (again, among only their qualifying members) open the doors for wrongdoing," the answer is "no" given the formidable rules already on the books to prevent against just that with respect to any partnership.

IV. Moving Forward With An Entity Agnostic Approach To Farm Bill Payment Limitations

The key to the authors' proposed entity agnostic approach to Farm Bill payment limitations lies in the name: simply make the entity form used by a farm operation irrelevant to its payment limitations. Put another way, treat any entity involving two or more parties like a partnership. Allow the entity to add up the payment limits of all its eligible members using all the existing rules for family members along with the AGI and AEF qualifications, and have those payments be attributed to the individuals using direct attribution and the four-level framework. Though much work would be needed to modify the implementing regulations and FSA guidance, the simplest statutory change would be:

> (1) Amend 7 U.S.C. § 1308(a)(3) to read: "The term 'legal entity' means an entity that is created under Federal or State law whose partners, members, or owners consist only of natural persons or the estates or trusts thereof and that . . .";[311]
>
> (2) Delete "or legal entity (except a joint venture or general partnership)" from 7 U.S.C. §1308(b) and (c);[312]

309. *See generally* FSA Handbook , *supra* note 74.
310. *See generally id.*
311. *See* 7 U.S.C. § 1308(a)(3).
312. *See id.* § 1308(b)–(c).

> (3) Delete 7 U.S.C. §1308 (e)(3)(B)(i);[313]
>
> (4) Renumber 7 U.S.C. §1308 (e)(3)(B)(ii) to become new 7 U.S.C. §1308 (e)(3)(B)(i) and change the first phrase to read "Payments made to a legal entity . . ."; and[314]
>
> (5) Renumber 7 U.S.C. §1308 (e)(3)(B)(iii) to become new 7 U.S.C. §1308 (e)(3)(B)(ii).[315]

Though it lacks the same punch as asking – "But what about Scottie Pippen?" – the proper agricultural policy wonk will immediately ask about the Congressional Budget Office (CBO) score. For the non-wonky among the readers, this means how will the CBO score the proposed change?[316] Without formal modeling, predicting the impact of the proposed rule on the Farm Bill's 10-year spending may be difficult. It is likely, however, that such change would be minimal for two important reasons. First, the proposed change does not affect who is eligible to receive Farm Bill payments. Remember, anyone receiving payments must still qualify under all the other existing Farm Bill rules. Thus, for the rule change to affect the quantity of Farm Bill payments, it would have to effectively induce new individuals to begin farming. If the proposed rule change does induce people into farming, it would indirectly fulfil the USDA's beginning farmer policy discussed above.[317] Second, as previously discussed, farmers are most likely operating with no limited liability protection as a partnership or are already using more complex entity structures by creating general partnerships comprised of multiple LLCs to accomplish what could be done under the proposed rule with simply one LLC or corporation.[318] As such, there will likely be marginal change in Farm Bill participation under the proposed rule change. The proposed rule simply makes things more straightforward and easier for farmers. Indeed, the USDA's FSA might see significant reductions in paperwork and recordkeeping as a result of the change.

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313. *See id.* § 1308(e)(3)(B)(i).

314. *See id.* § 1308(e)(3)(B)(ii).

315. *See id.* § 1308(e)(3)(B)(iii).

316. *See generally* Emily Stern, *CBO Explains How it Develops the Budget Baseline*, CONG. BUDGET OFF. (Apr. 2023), http://www.cbo.gov/publication/59085 [https://perma.cc/Q2RZ-MLJE] (providing a primer on calculation of CBO scores).

317. *See* discussion *infra* Section III.D.

318. *See* discussion *infra* Section III.B.4.

V. CONCLUSIONS

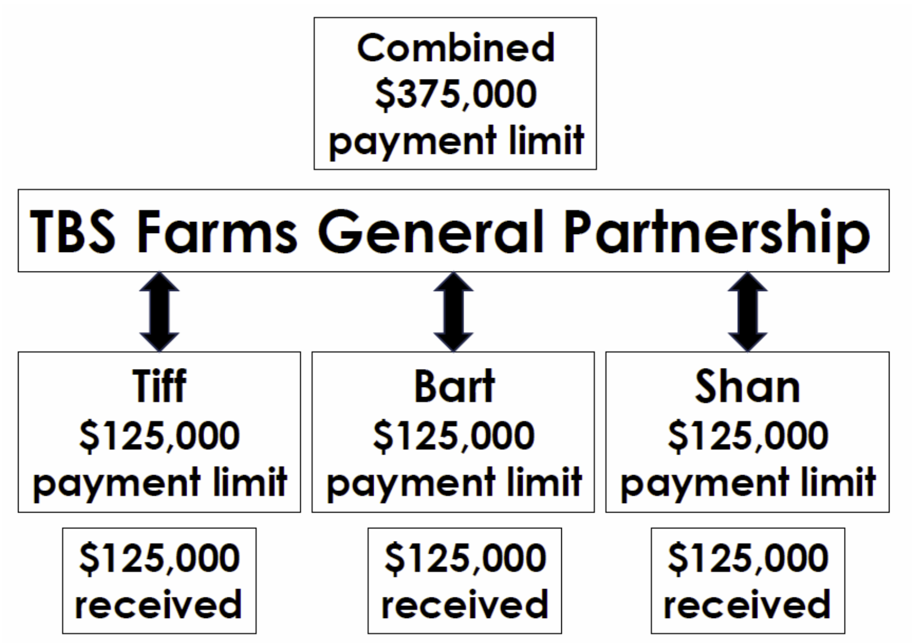
The Farm Bill's approach to risk management has changed significantly since 1933.[319] With those changes have come various approaches to farmer payments and the limitations on those payments. The Farm Bill's changes to payment limitations, eligibility, and the use of limited liability entities since 2008 appear to be a response to high-profile stories of wealthy individuals receiving Farm Bill payments.[320] While these changes may have been made with the best intentions, reactionary policy seldom provides good policy. A number of unintended consequences resulted from these changes thereby inhibiting the ability of modern farmers to manage an increasingly risky environment and effectively blocking access to powerful farm transition tools. An entity agnostic approach to Farm Bill payment limits is the best option. Current eligibility rules provide more than adequate safeguards to ensure those receiving Farm Bill payments are legitimately involved with their respective farming operations. With minor changes to the Farm Bill, and at virtually no cost to Congress, we can give farmers the best tools available to succeed both now and in the generation to come.

319. *See generally* Sidonie Devarenne & Bailey DeSimone, *History of the United States Farm Bill*, LIBR. OF CONG. (Oct. 2, 2023, 2:43 PM), https://www.loc.gov/ghe/cascade/index.html?appid=1821e70c01de48ae899a7ff708d6ad8b [https://perma.cc/D2ZM-CYD5].

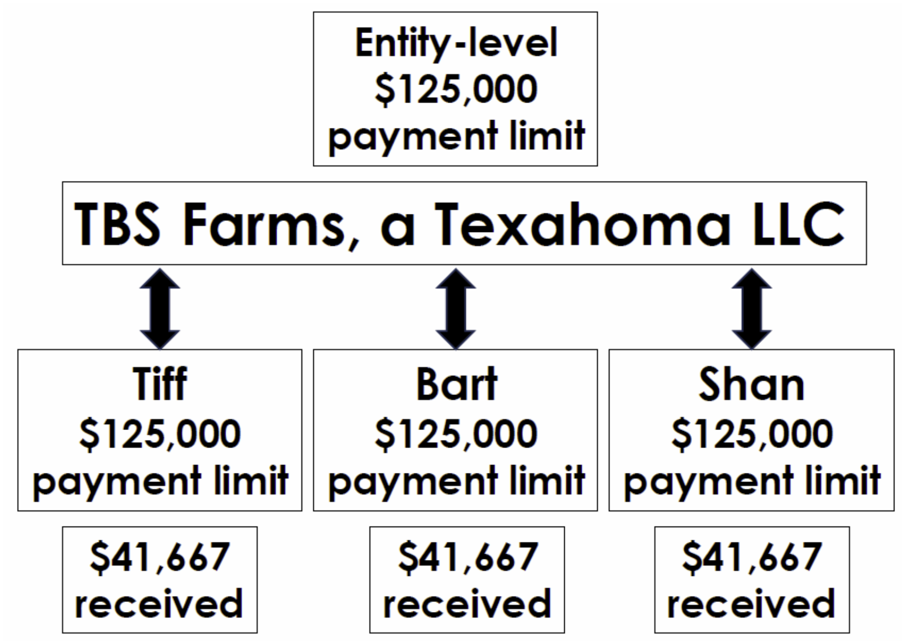
320. *See* Robert Coleman, *The Rich Get Richer: 50 Billionaires Got Federal Farm Subsidies*, ENV'T WORKING GRP. (April 18, 2016), https://www.ewg.org/news-insights/news/rich-get-richer-50-billionaires-got-federal-farm-subsidies [https://perma.cc/K4XR-FUYQ].

Appendix A: Entity Structure Examples

Example with PLC / ARC limits, general partnership



Example with PLC / ARC limits, LLC entity structure



Example with PLC / ARC limits, partnership formed with single-member LLCs