BUSINESS OPERATING AGREEMENT

The Farm Business Operating Agreement is the next step after the Enterprise Operating Agreement. This is often used as an intermediate arrangement between a wage arrangement and a partnership or corporation. Farm Business Operating Agreements are used when both parties contribute labor and management, have capital invested in the crop and/or livestock programs, and share the income generated from the farm operation.

The share of income received by each party depends on the contributions of each party. The party furnishing the largest share of resources will receive the largest share of the income. Only the parties involved can determine what is a fair return to each in view of the contributions of each party.

Costs and expenditures associated with owning individual assets are paid by the owner of the assets. For example, if the older generation provides the land and receives a payment in return (cash rent), then they are responsible for paying the property taxes and debt payments associated with the land.

Each party's income is used to pay the debt payments and expenses associated with individually owned resources contributed to the business. Additional income cam be used for family living expenditures and taxes, or additional investment in the business.

Changes in inventory can be included in the agreement. This requires more bookkeeping but provides a more accurate picture of income. Inventory also can protect one party from receiving undue financial benefits. Inventory adjustments can be calculated annually or once during the life of the agreement. They are computed by adding the year's-end or closing inventory to income and subtracting beginning inventory as a cost.

Example:

Sales	$165,000
Closing inventory	+23,000
Opening inventory	-19,000
Total Returns	$169,000

Adapted from Farm Savvy
Iowa State Extension
Step 2: Developing a Business Arrangement