The Evolving Legal Organization of California Farms: Corporations and LLCs

Hoy F. Carman

California corporate farms continue to grow in terms of numbers, share of all farms, acreage, and product sales. The average California corporate farm is larger than the average single proprietor and partnership farm, but all three organizational forms are represented in each of the size, asset and product sales categories from smallest to largest. Many California farms now realize some corporate advantages through organization as a Limited Liability Company.

The legal organization chosen for a farming business can have many implications. While any organizational model may be chosen at any stage in a firm's life cycle, most farms begin as single proprietor or family operations with some evolving into other forms as circumstances change. In general, income tax complexity, managerial requirements, and reporting rules increase as one moves from single proprietor to partnership to Limited Liability Company (LLC) to corporation.

Farm businesses typically have specific reasons to incorporate or become an LLC. For an LLC, the major reason is to gain limited liability by separating farm business operations and assets from personal assets. When a single proprietor or partnership changes to an LLC, their income tax treatment does not change and they have considerable flexibility in specifying firm management and allocation of revenues. Farm firms that incorporate typically do so for risk management and legal liability, separation of ownership and management, other management considerations, income taxation, employee benefit programs, inter-generational transfers of farm assets, and ownership of assets.

The Census of Agriculture, conducted on a five-year interval, presents annual data on farms by legal organization, including single proprietor or family farms, partnerships, corporations and others (cooperative, estate, trust, institutional, etc.). For the first time in 2012, the Census also counts the number of California farms registered as Limited Liability Companies (LLCs), often referred to as Limited Liability Corporations.

Corporate Farm Changes

California corporate farms continue to grow in both numbers and as a proportion of total farms. There were 6,361 corporate farms in 2012, a gain of 611 farms from 5,750 corporate farms reported in the 2007 Census (Table 1). The corporate gain of just over 1% of all farms, from 7.1% in 2007 to 8.2% in 2012, was the largest census-to-census percentage gain for corporate farms since 1978. Much of the growth in corporate farm numbers occurred between 1969 and 1982. There were 1,212 corporate farms in 1969 and 2,601 in 1974.

California farm corporations are characterized as being closely held by family members. Family members hold all the stock in 5,345 out of the total 6,361 farm corporations (84%), and 5,081 of these 5,345 farms have 10 or fewer stockholders. Overall, 93% of California's corporate farms (family and other than family held) have 10 or fewer stockholders.

While one must be careful about generalizations based on averages, California corporate farms can be characterized as having more land and other resources, and higher product sales, than individual or family farms and partnerships. In aggregate, corporate farms accounted for 21% of California's 25.6 million acres of land in farms and 35.3% of California's 2012 agricultural product sales.

Data on average farm characteristics in Table 2 illustrate the larger size of corporate farms. Corporations have the largest number of acres per farm at 843 acres, more than four times larger than the average 201 acres per farm for individual or family farms. Corporate average sales per farm are almost 11.6 times larger than average sales for individual or family farms. The corporate estimated market value of land and buildings, almost $6.3 million per farm, is more than five times the average for individual and family farms while the average value of machinery and equipment is six times higher for corporations.

However, all individual proprietor and family farms are not small, and not all corporate farms are large. For example, there are 1,020 individual and family farms with an estimated market value for land and buildings of over $10 million, and another 3,283 valued from $5 million to $10 million. There were 902 farm corporations with an estimated market

Table 1. Number of California Farms, Number of Corporate Farms, and Corporate Farms as a Proportion of Total Farms, Census Years 1978 through 2012

	Census Year							
	1978	1982	1987	1992	1997	2002	2007	2012
Total Farms	73,194	82,463	83,217	77,669	87,991	79,631	81,033	77,857
Corporate Farms	3,871	4,849	5,367	5,067	5,504	5,070	5,750	6,361
Corporate Farm Percentage	5.3%	5.9%	6.5%	6.5%	6.3%	6.4%	7.1%	8.2%

Source: USDA, Census of Agriculture for each year noted.

value for land and buildings of over $10 million, and another 684 valued from $5 million to $10 million. At the other end of the distribution, there were 3,768 individual and family farms and 198 corporations with an estimated value of land and buildings of less than $50,000.

Comparison of 2012 with 2007 corporate farm data shows some interesting changes. The average corporate farm increased from 784 to 843 acres, average product sales increased from $2,187,321 to $2,374,644, and the average value of machinery and equipment increased from $396,451 to $409,873. Despite increased acreage, the estimated market value of land and buildings for the average corporate farm decreased from $6,315,180 in 2007 to $6,255,875 in 2012. However, the corporation share of farms by number, with a value of land and buildings over $10 million, increased from 27.3% in 2007 to 29.8% in 2012. Conversely, the individual or family farms' share decreased from 39.4 to 33.7%.

Classification of Corporate Farms by Major Product

The Census of Agriculture uses the North American Industry Classification System (NAICS) to classify farms by the commodities that constitute a majority of the sales for the operation. One-half of California's corporate farms (3,187 out of 6,361) are fruit and tree nut farms. Corporate farms are 8.2% of all farms (Table 2) and 8.9% of all fruit and nut farms. Other NAICS farm classifications that include more than 8.2% corporate farms include greenhouse, nursery and floriculture farms (20.9%), cattle feedlots (12.8%), vegetable and melon farms (12.7%), dairy cattle and milk production (9.0%), and oilseed and grain farms (8.8%).

There is substantial variation in the market value of corporate farm sales, as well as the proportion of total sales by product category. Overall, the total market value of agricultural products sold and government payments for California farms was $42.6 billion in 2012. Of this total, family or individual farms accounted for $12.2 billion, (28.6 %); partnerships, $14.0 billion (32.8%); other farms, $1.4 billion (3.2%); and corporations, $15.1 billion (35.4%).

The product categories that have the largest proportion of corporate farm sales include: greenhouse, nursery, floriculture and sod (74.8%); vegetables, melons, potatoes and sweet potatoes (50.8%); berries (44.5%); cotton and cottonseed (36.9%); and fruit and tree nuts (36.8%). Farm product categories with the largest 2012 corporate farm sales included: fruit and tree nuts, $5.8 billion; vegetables, melons, potatoes and sweet potatoes, $3.2 billion; greenhouse, nursery, floriculture and sod, $1.9 billion; and cattle and calves, $1 billion.

Corporate Farm Operations

Census data provide some interesting observations on California corporate farm operations. While corporate farms had about 21% of California's land in 2012, they accounted for 30.3% of the irrigated land in farms. Almost 18% of all California farms enrolled just over 4.9 million acres of land in crop insurance programs during 2012. While partnerships had the highest participation (34.5%) and acreage enrolled (36.5%), just over 31.9% of California farm corporations accounted for 26.0% of the total acres enrolled in crop insurance programs.

Not surprisingly, corporate farms are an important employer for full- and part-time farm workers. The census reported that 4,167 farm corporations hired 92,613 workers for 150 days or more during 2012. This was about 45% of all farm workers who worked for 150 days or more during the census year. Farm corporations also hired about 35% of the 259,571 farm workers who worked less than 150 days during 2012. Almost 80% of California corporate farms reported hired farm labor in 2012, accounting for about $2.7 billion of the total payroll of $5.9 billion.

California farm corporations' role in organic farming is growing. The 2012 census reported a total of 3,008 California farms with organic sales totaling almost $1.4 billion. This compares with 3,515 farms with $656.8 million organic sales in 2007. There were 367 corporate farms with total organic sales exceeding $272 million in 2007. During the next five years, this increased to 482 corporate farms with total organic product sales of almost $686 million. Thus, corporate farm sales of organic products in 2012 were greater than total California farm sales of organic products by all farms in 2007.

Corporate farms accounted for about 41% of total organic product sales in 2007; this increased to 50.6% of California's organic product sales in 2012. The average corporate organic producer reported over $1.4 million of organic product sales in 2012. In contrast, 1,994 family or individual proprietor farms with organic production had average organic sales of $146,970 and accounted for just 21.6% of total 2012 organic sales.

California LLCs

The Census of Agriculture counted the number of California farms organized as LLCs for the first time in 2012, but did not report any details on their characteristics, size distribution, or operations. There were 4,453 California farms organized as LLCs in 2012. Of these, 2,096 (3.5%) of California's 59,732 family or individual proprietor farms were organized as LLCs, 2,111 (23.5%) of 8,984 California farm partnerships, and 246 (12.6%) of 1,949 other farms (cooperative, estate, trust, institutional, etc.) were LLCs in 2012.

A major reason for organizing a farm business as a corporation or LLC is that both offer "limited liability" to the business owners. This means that if the business has debts or faces a lawsuit for some other reason, only the business assets are at risk. With limited liability, creditors usually cannot reach the personal assets of the business owner. Since an LLC is sometimes described as offering the best features of a partnership and corporation, the legal organization of 23.5% of California's partnerships as LLCs is not surprising. LLCs offer considerable flexibility as to number and classes of owners, management, operations, and tax treatment.

According to California's Franchise Tax Board, forming an LLC in California is easier and faster than forming a corporation. In addition, LLCs do not issue stock and are not required to hold annual meetings or keep written minutes, which a corporation must do in order to preserve the liability shield for its owners.

For income tax purposes, an LLC is treated as a pass-through entity with a single member treated as a sole proprietor while an LLC with more than one member is treated as a partnership. Note that an LLC with either single or multiple members may elect to be taxed as a corporation by filing IRS Form 8832. Thus, an LLC can elect to be taxed as an S-corporation if the tax benefits of an S-corporation are considered advantageous. California LLCs are subject to an annual tax of $800 on California form 568, and may be subject to an additional LLC fee based on total income.

Table 2. California Farm Characteristics by Legal Organization, 2012

Descriptive Characteristic	All California Farms	Legal Status for Tax Purposes			
		Individual or Family	Partnership	Corporation	Other (coop, estate, trust, etc.)
Number of Farms	77,857	59,732	8,984	6,361	2,780
Percent of Farms	100	76.7	11.5	8.2	3.6
Average Size (Acres/Farm)	328	201	772	843	458
Average Sales/Farm	$549,397	$204,901	$1,565,016	$2,374,644	$492,826
Value of Land & Bldgs/Farm	$2,061,792	$1,228,827	$4,539,424	$6,255,875	$2,355,712
Average Value Machinery & Equipment	$124,720	$67,055	$308,970	$409,873	$116,232

Source: USDA, Census of Agriculture for each year noted.

Concluding Comments

California corporate farms are growing both in numbers and relative to other organizational choices. They are also getting larger, in terms of total acreage and acreage per farm, in per farm product sales, as well as share of total farm product sales.

One must be careful about general statements regarding corporate vs. individual proprietor or family farms. While the majority of California's farms with the smallest average land holdings and product sales are individual proprietor or family farms, some of these smallest farms are also partnerships and corporations.

There is substantial variation in crops grown and crop sales for different farms by legal organization. While involved in production of all California commodities, corporate farms tend to be most prevalent in some of the more capital intensive operations such as greenhouse, nursery and floriculture production, vegetable and melon farming, berry farms, and large fruit and tree nut farms.

Individual and family farms and partnerships tend to have more involvement in livestock and grain farms. Corporate farms account for over half of all California sales of organic products and their share is growing. Corporate farms are also a major employer for both full and part-time farm labor.

A relatively large number of California's family and individual farms and partnerships have recently organized as LLCs. This has probably reduced the number of farms that might have organized as corporations since organization as an LLC is an easier and less expensive option to gain limited liability protection for nonfarm assets. The future rate of incorporation of California farms is also expected to decline as the comparative features of LLCs and corporations become better known.

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Hoy F. Carman is a professor emeritus in the agricultural and resource economics department at UC Davis. He can be reached by email at carman@primal.ucdavis.edu.

For additional information, the author recommends:

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USDA. Census of Agriculture, State Level Data for California. Table 67. Summary by Legal Status for Tax Purposes: 2012. www.agcensus.usda.gov/Publications/2012/Full_Report/Volume_1,_Chapter_1_State_Level/California/st06_1_067_067.pdf