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## Tightening the Rules for Farm and Ranch Entities with Non-Family Members

-by Neil E. Harl\*

The Agricultural Act of 2014<sup>1</sup> directed the United States Department of Agriculture to define the term “significant contribution of active personal management” for purposes of the Food Security Act of 1985<sup>2</sup> and “. . . 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.”<sup>3</sup> The Secretary of Agriculture was under orders not to “. . . apply the regulations . . . to individuals or entities comprised solely of family members” and to apply the requirements of any resulting regulation “. . . beginning with the 2015 crop year.”<sup>4</sup>

The proposed regulations were published in the *Federal Register*<sup>5</sup> on March 26, 2015.

### Exceptions for Entities Comprised Solely of Family Members

As specified in the 2014 farm bill<sup>6</sup> that any new regulations would *not* apply to farming (and ranching) operations comprised of persons or entities involving *solely family members*, the proposed regulations respect that statutory limitation.<sup>7</sup> The new regulations state that “. . . all persons who are partners, stockholders, or persons with an ownership interest in the farming operation or of any entity that is a member of the farming operation are family members. . . or the farming operation is seeking to qualify only one person as making a significant contribution of active personal management for the purposes of qualifying only one person or entity is actively engaged in farming.”<sup>8</sup>

### Farming Operations With Nonfamily Members

If a farming operation includes *any* nonfamily members and the farming operation is seeking to qualify more than one person as providing a significant contribution of active personal management, then (1) each such person must maintain contemporaneous records or logs as specified. . . and (2). . . if the farming operation seeks not more than one additional person to qualify as providing a significant contribution of active personal management because the operation is large, then the operation may qualify for one such additional person if the farming operation (a) produces and markets crops on 2,500 acres or more of cropland; or (b) for farming operations that produce honey with more than 10,000 hives; or (c) for farming operations that produce wool with more than 3,500 ewes, and (3) if the farming operation seeks not more than one additional person to qualify as providing a significant

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contribution of active personal management because the operation is complex, then the operation may qualify for one such additional person if the farming operation is determined by the FSA state committee as complex after considering the factors specified in the regulations.<sup>9</sup> If a farming operation seeks to qualify a total of three persons as providing a significant contribution of active personal management, then the farming operation must demonstrate both size and complexity to obtain approval.<sup>10</sup> However, *in no case may more than three persons in the same farming operation qualify as providing a significant contribution of active personal management.*<sup>11</sup>

### Economic Consequences of the Proposed Regulations

The Department of Agriculture estimates that roughly 1,400 joint operations could lose eligibility for around \$50 million in total crop benefits for the 2016 to 2018 crop years from the Price Loss Coverage (PLC), Agricultural Risk Coverage (ARC) and Marketing Assistance Loans (MAL) programs, ranging from \$38 million for the 2016 crop year down to approximately \$4 million for the 2018 crop year. The economic consequences depend upon prices and yields under the various programs of course.

The proposed regulations do not change the payment limitation per person which is a joint \$125,000 for the various programs.

The official explanation notes that the \$125,000 payment limit per person applies to general partnerships and joint operations based on the number of eligible partners in the operation. That is to say, each partner may qualify for a separate payment limit of \$125,000. Stated differently, each person in the partnership or joint operation who loses eligibility because of the proposed regulations will lose eligibility for up to \$125,000 in payments. Other types of entities, such as corporations and limited liability companies (LLCs), that share a single payment limit of \$125,000, regardless of the number of owners, would not have their payments reduced by the regulations. Once again, entities comprised solely of family members would not be impacted by the proposed regulation.

### New Definition of Significant Contribution of Active Personal Management

The existing definition of a “significant contribution”<sup>12</sup> specifies that for active personal management, a significant contribution includes “activities that are critical to the profitability of the farming operation”<sup>13</sup> but that definition does not specify what specific types of activities are included, whether those activities need to be direct actions and not passive activities, and to what level or degree such activities must be performed to achieve a level of significance.

The proposed regulations would apply a new definition of “significant contribution of active personal management” but only to non-family farming operations that are seeking more than one farm manager.<sup>14</sup> The proposed regulations add a new, more specific definition for “active personal management” that includes a list of critical management activities that may be used to qualify as a significant contribution under one or more of several categories including – (1) capital, which includes (a) arranging financing and managing capital, (b) acquiring equipment, (c)

acquiring land and negotiating leases, (d) managing insurance and (e) managing participation in USDA programs; (2) labor which includes hiring and managing hired labor; and (3) agronomics and marketing, which includes – (a) selecting crops and making planting decisions, (b) acquiring and purchasing crop inputs, (c) managing crops (that is, whatever it takes to keep the growing crops living and healthy including soil fertility and fertilization, weed control, insect control, irrigation (if applicable) and making harvest decisions, and (d) pricing and marketing of crop production.

The proposed regulations go on to state that “significant contribution of active personal management” means active personal management activities performed by a person with a direct or indirect ownership interest in the farming operation on a regular, continuous and substantial basis to the farming operation and meets at least one of the following to be considered significant – (1) performing at least 25 percent of the total management hours required for the farming operation on an annual basis, or (2) performing at least 500 hours of management annually for the farming operation.<sup>15</sup>

### ENDNOTES

<sup>1</sup> Pub. L. No. 113-79, § 1604, 128 Stat. 649 (2014). See generally 11 Harl, *Agricultural Law* Ch. 91, App. 91C (2014).

<sup>2</sup> Pub. L. No. 99-198, 99 Stat. 1430 (1985). See 11 Harl, *Agricultural Law* § 91.03[1][e] (2014).

<sup>3</sup> Pub.L. No. 99-198, 99 Stat. 1430 (1985). See 7 U.S.C. § 1308-1.

<sup>4</sup> Pub. L. No. 113-79, § 1604, 128 Stat. 649 (2014). However, in the 7 CFR commentary on economic impacts, the examples appear to be assuming the effective date would be 2016.

<sup>5</sup> 80 Fed. Reg. 15,916 (March 26, 2015).

<sup>6</sup> See note 4 *supra*.

<sup>7</sup> 7 CFR Part 1400, 7 U.S.C. § 1308, 1308-1, 1308-2, 1308-3, 1308-3a, 1308-4, 1308-5. See 7 CFR § 1400-600(c).

<sup>8</sup> 7 CFR § 1400.600(c).

<sup>9</sup> 7 CFR § 1400.602.

<sup>10</sup> 7 CFR § 1400.602(c).

<sup>11</sup> 7 CFR § 1400.602(d).

<sup>12</sup> 7 CFR § 1400.3.

<sup>13</sup> *Id.*

<sup>14</sup> 7 CFR § 1400.601.

<sup>15</sup> *Id.*