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# Owning and Protecting a Farm, Ranch or Fishing Business

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# Partners in Tax Education

California FarmLink is proud to offer this webinar with financial support provided by the USDA Farm Service Agency Tax Education and Asset Protection Initiative using funds Congress allocated for this purpose in the American Rescue Plan Act (ARPA).



# About the Instructor

Poppy Davis is a business and policy adviser to agricultural enterprises, nonprofits, and local governments. She works through programs around the country to deliver trainings on topics including agricultural taxation, accounting, credit, and cash-flow.

She began her career as a California CPA, and later worked for the USDA.

She holds a Juris Doctor with a certificate in Food and Agricultural Law from Drake University Law School, and a BS in Agricultural Economics from the University of California at Davis.



# Overview

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1. Structure
2. Ownership and Capitalization
3. Contributions and Liability
4. Asset Protection Strategies

**Note: This presentation is not intended for organizations operating as not-for-profits.**



# Structure

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# What do we mean by “Business Structure?”

**Structure is the way a business is owned, how owners buy in, how profits are shared, how assets are used, and how liabilities are limited and shared. It includes:**

- Legal form of ownership of business, assets
- Capitalization or owners’ buy-in
- Asset protection and risk management  
Strategies to protect the assets of the business and manage risk of loss or liability



# Ownership and Capitalization

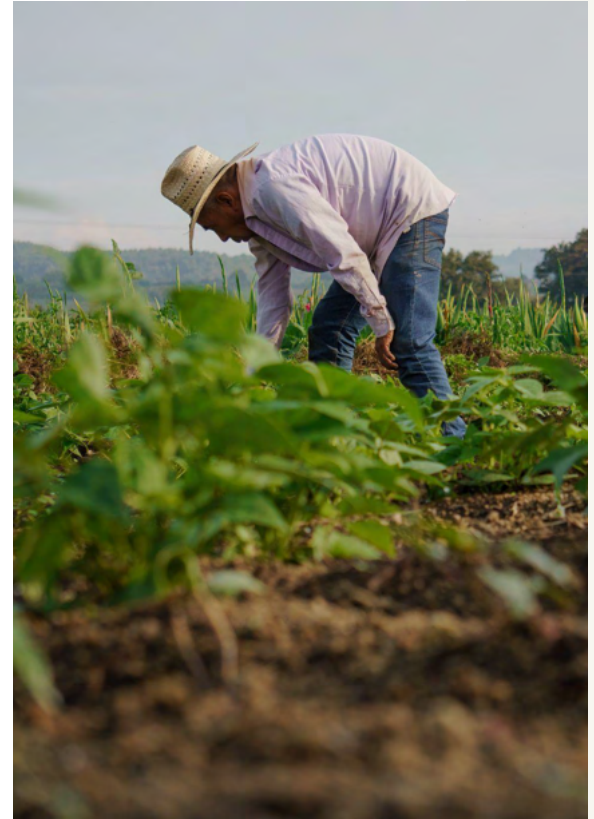
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# What does it mean to own a business?

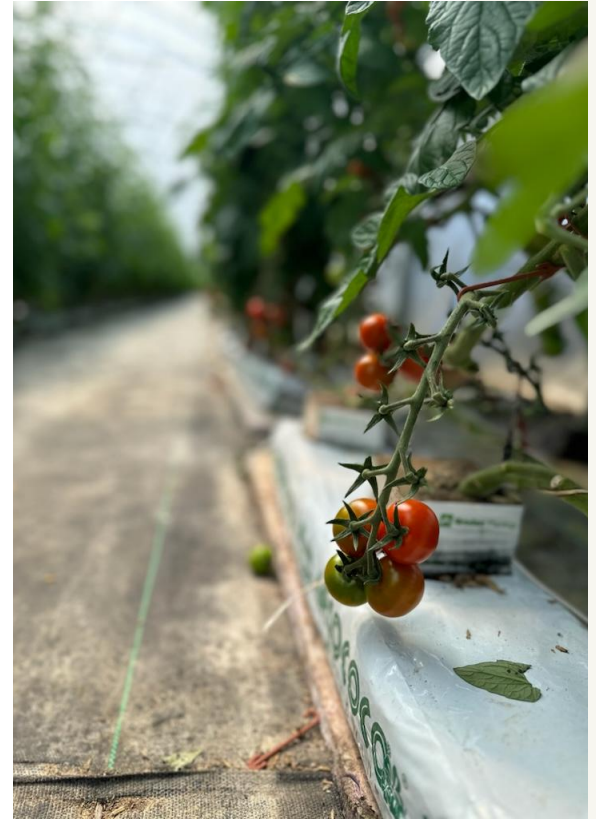
**A business owner has invested capital and is entitled to receive a share of profits.**

- The legal form of ownership will determine how the owner makes their investment of capital and how profits or losses are shared.
- Depending on the legal form of ownership, there may be documents that specify how owners are entitled to direct the activities of the business.



# The Legal Form of Business Ownership

- **Sole Proprietorship** is the default legal ownership for a single owner.
- **General Partnership** is the default legal ownership for more than one owner.
- **Limited Partnership, Limited Liability Company, and Corporation** are forms of legal ownership that must be deliberately created under state law.



# Business Entities

- Informally we say that the legal form of a business is the entity type.
- Formally a business is a separate legal entity if it can sue and be sued separately from its owners.
  - These formal business entities include Limited Partnerships, Limited Liability Companies, and Corporations.



# What is capital?

**The resources that allow you to operate your business.**

- Cash
- Equipment
- Labor
- Land and natural resources
- Knowledge (technical, processes, procedures)

**Credit, leases, and labor agreements are all ways to access capital beyond the owners' original contributions of capital.**



# Capitalizing a Business

**Owners capitalize a business by contributing cash, or other assets like land or equipment.**

- A business plan provides a preliminary assessment of the cash and credit needs of a business taking into account owners contributions and ability to access credit.
- If a business does not have enough cash it is “under-capitalized” and may have to take on debt.



# Contributions and Liability

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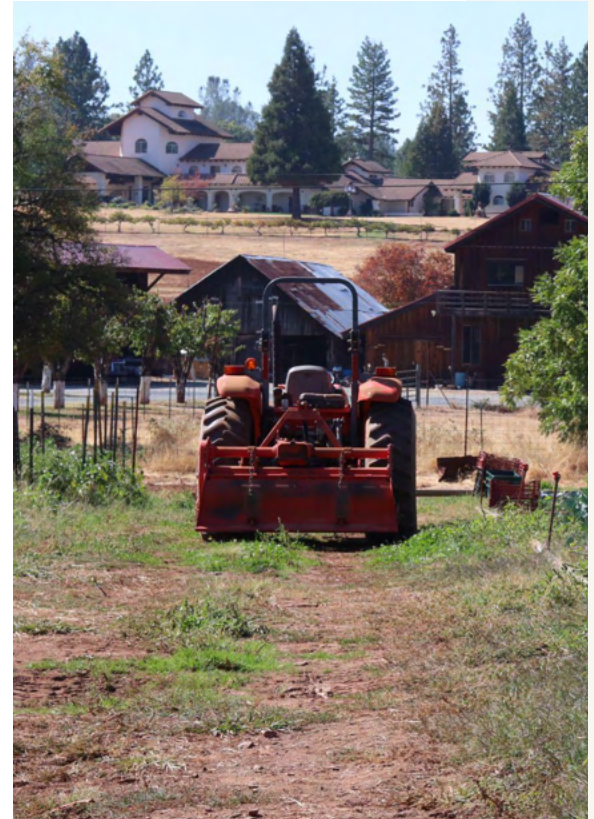


# At-Risk Capital

**Once an owner invests their capital (usually cash and equipment) into a business, that investment is at risk - it may be used to:**

- Fund unprofitable activities
- Repay debts that can not be paid from business profits
- Settle legal claims against the business

At-risk capital is also called ***invested capital***, because one of the key qualities that makes something an investment is the risk of loss.



# Unlimited Personal Liability

**In addition to invested capital, owners of a sole proprietorship or a partnership also have unlimited personal liability for debts, fines, penalties and legal judgments against the business.**

- May have to use personal savings
- May have future wages garnishes
- Liability may extend to a spouse's savings and future earnings

**In a partnership each partner (and their spouse) is liable for all of the obligations of the business. If other partners cannot pay the partners who can must - and then it is up to them to collect from the other partners if they can.**

# Limited Liability

**Business owners may limit their liability to only their at-risk capital by forming a business entity that is intended to protect the owners from unlimited personal liability:**

- A limited partnership
- A limited liability company
- A corporation

These entities are formed under state\* law and may provide liability protection across state lines and under federal law. These entities will never protect an owner from the risk associated with negligence or deliberate bad acts.

\*In some cases may be formed under Tribal law or directly under federal law.

# Ownership Rights and Obligations

**A business plan discusses the owners rights and obligations including the legal structure and key terms in the operating agreement covering:**

- The amount of cash each owner will initially contribute
- The owners' rights to direct and manage the business, and decision-making authority if there is more than one owner
- Circumstances under which an owner may be required to contribute additional cash
- Limitations on how much owners may withdraw
- Circumstances under which an owner may withdraw capital from the business
- Restrictions on the sale or transfer of ownership interests
- How profit and loss will be shared

# Asset Protection Strategies

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# Separate Assets from Risk

Part of structuring a business is ensuring that valuable assets are owned outside of the entity that conducts the day-to-day activities of the business.

- The **operating entity** engages in activities - and with that comes risk.
- The **land-owning entity** rents the land to the operating entity - a low-risk activity.
- If the operating entity gets into financial or legal trouble the owners may lose all of their at-risk capital - but that does not include the land because it is not part of the operating entity.



# Obtain Property and Liability Insurance

A business plan should discuss the appropriate insurances needed to protect the assets of the business, and the budget should include an adequate amount to cover property and liability insurance.

- Property insurance provides an indemnity if the property is lost or damaged due to an insurable cause of loss.
- Liability insurance covers the cost of legal defense and settlement if there are damages due to a business activity.



# Plan and Prepare

A business plan should include preliminary plans to ensure worker and product safety, emergency preparedness, and regulatory compliance.

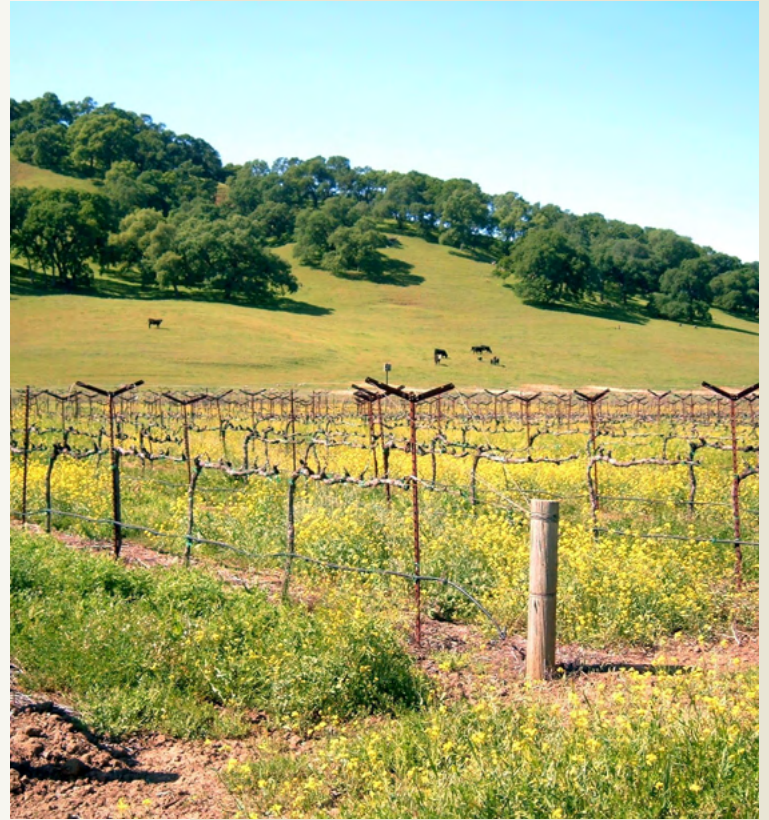
<b>Increase</b>	<b>Decrease</b>
Worker safety	Injury, damage, lawsuits
Product safety	Injury, lawsuits, fines
Emergency preparedness	Injury and loss
Regulatory compliance	Penalties, fines, headaches



# Action Plan to Strengthen Resilience

The template in the FarmLink Business Planning Learning Center will help you assess your business and make an action plan.

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# Questions?

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# Thank you!

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