

## **Farm Land Transfer Using a Limited Liability Company**

We will use the following business terms to discuss a scenario in which a farmland owner, Janet Brown, has reached a point where she wants to retire from farming but has no family willing to take over the farm operation. She has employed a young woman on the farm, Marcelle Vargas, over the last few years who is very interested in continuing to farm the land and ultimately purchase the farmland from Janet. Marcelle does not have a lot of financial resources but is a hard worker and willing to enter into an agreement that will commit her to working and acquiring ownership over a period of time. We will discuss how to memorialize the terms into an operating agreement, a farm lease and a purchase option.

### **Structure**

- Formation of a new limited liability company (the “Company”) to lease farm land with ultimate transfer, from Farm Land Owner, Janet Brown (“Brown”) to the Farmer, Marcelle Vargas (“Vargas”).
- Equity ownership in the company will come in two forms: Class A membership interests and Class B membership interests.
  - Class A interests will be held by Brown as the “Managing Member” of the Company, with the right to take any and all actions on behalf of the Company.
  - Class B interest will be held by Vargas as the “Operating Member”, with day-to-day operational responsibilities for the Company.
  - 100% of rental income of the Company will be allocated to Class A membership interests, along with 100% of other distributable cash (from capital contributions, see below).
- Company cannot sell the property without written consent of Vargas prior to end of the Purchase Option Exercise Period (see below).

### **Company**

- Brown contributes 100% of the fair market value of the property as its capital contribution, and receives one Class A share for each \$1,000 of capital contributed.
- Vargas contributes capital to the company equal to 10% of the net purchase price of the property, and receives one Class B share for each \$1,000 of capital contributed.
- At closing, the Company acquires the property or properties and enters into a 9-Year lease with Vargas as governed by a separate agreement (the “Lease Agreement”).



### **Payments**

- Vargas is responsible for paying all taxes (including property taxes), insurance, and other expenses for maintenance and operation of the property.
- In addition to covering the above expenses, Vargas makes monthly rental payments to the Company at an annual rate of \$\_\_\_\_\_ as governed by the Lease Agreement.
- Starting the \_\_\_th month after Closing and continuing until the end of the expiration of the Lease Agreement, Vargas makes additional annual capital contribution payments at an annual rate of \$\_\_\_\_\_ [or \_\_\_% of Vargas' gross sales for the year]. These payments can be deferred in the event Vargas' gross sales in any year are less than \$\_\_\_\_\_.
- The capital contribution is sized such that Vargas will increase her equity ownership of the Company from 10% at closing to 100% in year 9, assuming all payments are made.
  - The Managing Member of the Company distributes 100% of these additional capital contributions to the Class A holders. These distributions are considered a return of capital, redeeming Class A membership interests and thereby reducing the Class A holders' percentage ownership of the Company.

### **Value of Class A Shares**

- The purchase price for each Class A share of the Company will appreciate at 3% per year, compounding annually. Such that after one year, the Vargas receives one Class B share for each \$1,030 of additional capital contributed; after two years, Vargas receives one Class B share for each \$1,060.90 of additional capital contributed; after three years, Vargas receives one Class B share for each \$1,093.73 of additional capital contributed; etc.

### **Purchase Option**

- On the 5<sup>th</sup> anniversary of closing and at the expiration of the Lease Agreement, Vargas can exercise an option (each a "Purchase Option") to buy all of the remaining Class A membership interests and take sole ownership of the Company.

### **Farmer Default**

- Failure by Vargas to make rental payments, tax payments, additional capital contributions, achieve certain agricultural and land clearing milestones, and violating property use covenants, would constitute a Default.



- In the event of Default, Brown will take over operations of the Property, and will either manage the property directly or attempt to find a new operating partner to manage the Property.
- Vargas will retain its ownership interest in the company's Class B shares; any amounts owed or still payable by Vargas under the Lease Agreement at the time of Default, including rent and property taxes, would be calculated and this total amount ("Default Payment") would be charged against Vargas' Class B membership interest.
- In the event that the Lease Agreement can be assigned to, or a new agreement signed with, a new operator ("New Farmer"), Vargas' Default Payment would be reduced to the extent that New Farmer assumes financial obligations.

### **Sale of Property**

- If (i) Vargas is in Default under the Lease Agreement; or (ii) if Vargas does not exercise a Purchase Option before the end of the Lease Term, and the parties have not agreed to an extension of the Lease Agreement; then Brown has the right to sell the Property.
- In the event of sale of the Property, all net proceeds from sale will be distributed on a pro-rata basis between Vargas and Brown, based on each party's membership percentage at time of sale.

