General Partnership Agreements for Cattle Producers

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At one point or another, most cattle operations form a partnership with another person or entity. Perhaps it is a partnership on a single head of cattle (e.g., a flush cow, a bull in a stud, a show heifer) or perhaps it is a more long-term partnership where profits and losses will be shared among family members or cattle operations. Cattle owners have many choices in business organizations such as limited liability partnerships, limited liability companies, corporations, and trusts. The purpose of this article is to concentrate on the general partnership and discuss what language should be included in a partnership agreement.

Overview of General Partnerships

Among every type of business organization, the general partnership also offers cattle producers the greatest flexibility. As a caveat, the general partners are jointly and severally liable for the debts of the partnership whereas other types of formal business entities may shield owners from personal liability (i.e., the "corporate shield"). Another drawback of a general partnership is the lack of flexibility with ownership transfers. By default, general partnerships require unanimous consent before that interest is transferred. For longterm business ventures, it is recommended that cattle producers talk to their accountant and an attorney to see if a formal business entity is appropriate.

There are no particular formalities required to form a general partnership. The partnership agreement does not necessarily have to be in writing nor does the agreement have to use the words "partnership" or "partner." An agreement to share profits creates a presumption that a general partnership exists between the parties. Therefore, profits should not be shared with employees unless a partnership is intended. If a cattle operation wishes to give employees a percentage of profits, a contract should be written clearly enumerating the ownership interests (or lack thereof) of the parties.

Most states have enacted state statutes that provide "default rules" for partnerships such as management rights and a partner's share of the profits and losses. Even though these default rules are in effect, the partners can change any of the default provisions by written agreement. Unless otherwise agreed in writing, by default partners have equal management authority and entitled to an equal share of profits and losses. To illustrate, a retired cattle owner may wish to no longer manage the operation but offers his $1 mil. capital in land, buildings and cattle to a herdsman who will front $50,000 to help maintain the operation. If there is $200,000 profits in Year 1, by default each of the two partners will equally share the profits despite the unequal contributions. Similarly, if the operation had lost $25,000 that first year each of the two partners would be equally liable for this loss under most state's default rules.

Suggested Provisions in a Partnership Agreement

It is recommended that partnership agreements be in writing and drafted by an attorney; however, it is understandable that there are circumstances where it is not economical to pay for legal fees some business agreements. Even so, cattle producers should get the terms of their agreement in writing to formalize the terms and to help prevent future disputes. Some provisions that should be considered in the partnership agreement include the following:

1. Names and addresses of the partners. This section in the partnership agreement should include the names of any formal business organizations (e.g., Curt Rincker D/B/A Rincker Simmentals and Blackacre Ranch, LLC).

2. Name of the Partnership. This may not be necessary for partnerships with only one or two head of cattle but a name of a partnership is encouraged. Before deciding on a partnership name, make sure you are not infringing on a trademark. The partnership agreement should also consider whether the name will remain for continued use after a partner dies. Any restrictions for use of the name for any other activities should be noted. For example, a farm family may decide to draft a formal partnership agreement under the name of Rincker Cattle Co. for raising seedstock cattle but restrict the use of the name for agritourism efforts.

3. Purpose of the Partnership. It is important to include the purpose and scope of the partnership agreement and enumerate authorized business activities. For example, the purpose of the partnership may be to produce club calves out of thirty designated cows while authorized business activities includes advertising and marketing.

4. Term of the Partnership. The term of the partnership should be narrowly defined. For example, will the partnership agreement last for certain number of years, until a certain head of cattle dies or is sold, or until one of the partners dies? The partnership could also end when one party is in default for a certain period of time (e.g., failure to pay maintenance or operating expenses for 90 days).

5. Initial Contribution of Each of the Partners. The partnership agreement should clearly define the amount of money each partner should contribute initially and list instructions on how and when that payment should be delivered. The initial contribution could be in the form of cash, property or services. To demonstrate, CBR Cattle was formed and “C” gave the partnership $2 mil worth of land and equipment while “B” contributed $300,000 worth of cattle for the partnership’s use. “R” was hired as the herdman to run the ranch, work on salary and keep a small portion of the profits. A graphics design company was a silent partner who developed the partnership’s website for a percentage of the profits. Each of these four partners have very different initial contributions to the partnership in terms of cash, property and services.

6. Additional Contribution Requirement. After the initial contribution, any other required maintenance or required payments or services should be provided in the partnership

agreement. For example, each partner may be obligated to pay $2,000 a month for operating expenses. Alternatively, in the above example, perhaps the graphics design company is required to develop monthly magazine ads and coordinate daily social media efforts of the partnership for its share of the profits. The partnership agreement should also discuss any interest owed for outstanding payments or services promised, give directions for the timing and delivery of payment, and note any notice requirement for unanticipated expenses.

7. Assets of the Partnerships. Understandably, enumerating a complete list of partnership assets may be onerous for some large cattle operations but it is important to itemize and accurately describe the assets of the partnership in the agreement itself. This not only assists in the valuation of a partner's contribution but also mitigates future disputes and confusion during the winding up stage.

8. Liability of the Partnership. The agreement should include the liability that the other partners have to one another. For example, will partners indemnify each other for their own negligent acts that have harmed the partnership's property and/or third parties?

9. Allocation of Profits and Losses. Unless agreed upon differently, profits and losses will be shared evenly among the partners. If there is a salaried partner who does not share in losses, this should be specifically addressed in this section. Perhaps a partner who fronts all maintenance and marketing expenses on a show bull will want to keep 60% of the profits from semen sales and 100% of show winnings. Whatever your agreement is, it should be memorialized in the agreement to avoid a disagreement later on.

10. Distribution of profits. Distribution and allocation of profits are different concepts. Typically, some profits may go back into the partnership to help with operating expenses or growth. "Distribution" is identified as the actual pay-out of the profits. The agreement should enumerate procedures for making the distribution, ability to receive advance payments or draws from anticipated earnings, identification of person(s) that will declare the distributions, and timing of distributions. Furthermore, any limitation on distributions should be memorialized.

11. Duties of the Partners. The partnership agreement should not only specifically address the responsibilities required by each partner but also prohibition of activities. For example, one partner may be in charge of the care and maintenance of a flush cow while the other partner makes all management decisions with artificial insemination and marketing. Additionally, any confidentiality concerns should be addressed such as trade secrets. For example, Cattle Producer A might not want Cattle Producer B to disclose to third parties his/her feed rations, business relationships, or actual sale price of embryos made known through the partnership.

12. Salaries and Other Benefits of the Partners. Not only should the salaries be properly memorialized, but vacations, holidays, retirement, health insurance and other benefits should also be discussed in the partnership agreement. If a cattle producer goes on a family

vacation for a week after the Houston Livestock Show and Rodeo, is it okay for the neighbor kid to feed and care for the cattle owned by the partnership? Should one partner owe another partner any type of notice before such vacations? These types of issues should be discussed.

13. Expenses of Partnership. It is important to establish all the anticipated expenses of the partnership. To illustrate, perhaps an expensive show heifer was purchased to be flushed for embryo transplants. Even though each partner initially contributed 50% of her sale price, there are other potential expenses in maintaining this female including feed, veterinary care, shelter, flush expenses, semen, travel and advertising costs. Even though each partner may informally decide to pay 50% of all these expenses, these costs should be enumerated in the partnership agreement in case one partner later decides that he cannot afford his/her share of the fees.

14. Management of the Business. If a particular partnership is to be managed by less than all the partners, the agreement should identify the managing partners. For example, perhaps ten businessmen in Oklahoma decide they want to invest monies in the cattle business but know very little about the industry. These businessman find Rockin' R Cattle, Inc. to invest $200,000 on commercial feedlot cattle. Rockin' R Cattle, Inc. should be identified as the managing partner while the Oklahoma businessmen still receive a certain percentage of the profits.

15. Effect of a Default. The partnership agreement should discuss what will happen if one or more partners is in default after a certain period of time. If one partner fails to pay his/her half of the rent in a bull stud, will that partner then forfeit his right to make management decisions? Should the partner(s) give the defaulting partner some kind of notice and time to cure a default before management rights are affected?

16. Amendments to Partnership Agreement. For both long and short-term business ventures, it is unrealistic to think that partnership agreements will not need to be amended. Family operations grow, life has unexpected twists, and business plans change. The partnership agreement should allow for amendments to be made in writing by a certain percentage of the votes from the partners.

17. Partner Changes. The partnership agreement should discuss the process for voting on any additional or substitute partners and any redistribution of assets in such an occurrence. There should also be provisions discussing the procedures for the withdrawal or removal of a partner and any limitations on a voluntarily withdraw. Buy-out prices should be noted in the partnership agreement in addition to the consequences of a partner's death.

18. Assignability. The agreement should enumerate any limitations on the ability to sell his/her ownership interest to another. For example, the partnership agreement could give the other partner(s) first right of refusal or limit the pool of sellers in some way (e.g., restrict the sale to a competitor).

19. Alternative Dispute Resolution ("ADR"). Arbitration and mediation can in some cases be less costly and faster than the traditional court system. Some states offer an affordable agriculture mediation program that can be particularly useful if there is an even number of partners where there may be a dead-lock in the vote.

20. Forum Selection. The partnership agreement can identify a particular court where disputes must be tried. It is recommend to choose a neutral location that is equally convenient for all parties.

21. Choice of Law. Partnership law is state law issue. If a partnership is created among partners of more than one state then the agreement should identify whose state law applies to enforce the partnership agreement and "fill in the gaps" where the agreement is silent.

22. Attorneys' Fees. Should a dispute arise between partners, it is recommended that the losing partner be obligated to pay the other partner(s) for attorneys' fees. Furthermore, payment of legal services required in the course of the partnership should be decided upon.

23. Dissolution and Winding Up. The agreement should enumerate facts and circumstances that may lead to the dissolution of the partnership (e.g., death of partner(s), death/sale of cattle, withdraw of a partner, insolvency) and procedures for winding up the business including distribution of assets.

Finally, it is very important to tailor your partnership agreement to your particular needs. It may be useful to identify agreed upon veterinarians, embryologists, financial institutions for partnership loans, feeding programs, herdsmen and hired help, cattle shows to regularly participate in, magazines to place monthly ads in, approved photographers, approved sires for artificial insemination, payment of registration papers a breed association or membership to the National Cattlemen's Beef Association, or responsibility to develop an employee handbook and/or train employees of proper animal handling. Tweak your partnership agreement for each specific business venture. When in doubt, err on the side of detail in your agreement.

More Than A Handshake

Even though cattle folk are the most honest hard-working people on earth, a handshake will not properly protect a cattle producer in court should a dispute arise. Not only is it a sound business practice to get partnership agreements in writing but it may salvage longterm relationships with people when a dispute arises. Unexpected things happen outside of the control of all parties that may create a disagreement (e.g., eminent domain or Acts of God). Partnerships are at the mercy of their state's default rules unless agreed upon in writing. Cattle producers are encouraged to get a general partnership agreement in writing and seek professional guidance from an attorney licensed in that jurisdiction. If you cannot afford legal guidance, you should nonetheless memorialize the terms of the agreement even if the business venture is with a lifelong trusted cattlemen.