Types of agribusiness

Lecture 2

Introduction

- An agribusiness may be a firm with billions of dollars of sales that employs thousands of people, or it may be as small as an individual who is a part-time seed corn salesperson. Agribusinesses may engage in a variety of activities that are related to the production, processing, marketing, and distribution of food and fiber products.

- Though the one-person or one-family agribusiness is not uncommon, most of the actual business volume in agribusiness is conducted by enterprises that employ hundreds or even thousands of people.

Introduction

- Every agribusiness is owned by someone, and it is the circumstances of ownership that give an organization its specific legal form. There are five basic business forms:
    - sole proprietorship,
    - partnership,
    - corporation,
    - limited liability company (LLC), and
    - cooperative.

Factors influencing choice of business form

1. What type of business is it, where will it be conducted, and what are the owners’ objectives and philosophies for the agribusiness?
2. How much capital is available for the firm’s start-up?
3. How much capital is needed to support the agribusiness?
4. How easy is it to secure additional capital for the agribusiness?
5. What tax liabilities will be incurred and what tax options are available?

The sole proprietorship

- The oldest and simplest form of business organization is the **sole** or **individual proprietorship**, an organization owned and controlled by one person or family. It is the most popular business organization. All profits and losses, all liability to creditors and liability from other business activities are vested in the proprietor.
- The legal requirements necessary to organize as a sole proprietorship are minimal. About all that is required is an individual's desire to start a business and the purchase of a license, if one is required for that particular kind of business
- The **proprietorship** gives the individual owner complete control over the business, subject only to government regulations that are applicable to all businesses of that particular type. The owner exerts complete control over plans, programs, policies, and other management decisions.

The sole proprietorship

- Perhaps the most important disadvantage of the proprietorship is the owner's personal liability for all debts and liabilities of the business, which can extend even to the owner's personal estate. In a proprietorship, there is no separation between business assets and personal assets. Consequently, this form of business organization is characterized by what is called unlimited liability.

- The owner's liability does not stop with business assets; it also extends to personal assets. Another important disadvantage relates to the generally limited amount of capital funds that one person can contribute. Lenders are also somewhat reluctant to lend to an individual owner unless the owner's personal equity can guarantee the loan. Proprietorships often find that they are starved for capital, and this serious disadvantage may do more than stunt growth.

Partnerships

- A **partnership** is the association of two or more people as owners of a business. There is no limit to the number of people who may join a partnership. Apart from the fact that a partnership involves more than one person, it is similar to the proprietorship. Partnerships can be based upon written or oral agreements, or on formal contracts between the parties involved.

- There are basically two kinds of partnership:
  - general partnerships
  - limited partnerships.

General partnerships

- In a **general partnership** , each individual partner — regardless of the percentage of capital contributed — has equal rights and liabilities, unless stated otherwise in a partnership agreement.

- A general partner has the authority to act as an agent for the partnership, and normally participates in the management and operation of the business. Each general partner is liable for all partnership debts, and may share in profits, in equal proportion with all other partners. If the partnership struggles and has financial problems, all liabilities are shared equally among the partners for as long as sufficient personal resources exist.

General partnerships

- when one partner’s resources are exhausted, remaining parties continue to be liable for the remaining debt. General partners may contract among themselves to delegate certain responsibilities to each other, or to divide business revenues or costs in some special manner (e.g., according to funds invested or job responsibility).
- Each general partner can bind the partnership to fulfill any business deal made. While the partnership is usually treated as a separate business for the purposes of accounting, it is not legally regarded as an entity in itself, but as a group of individuals or entities.

Limited partnership

- All partnerships are required by law to have at least one general partner who is responsible for the operation and activities of the business, but it is possible for other partners to be involved in the business on a limited basis.

- A **limited partnership** permits individuals to contribute money or other ownership capital without incurring the full legal liability of a general partner. A limited partner’s liability is generally limited to the amount that the individual has personally invested in the business.

Partnerships

- Partnerships are just about as easy to start as proprietorships. They require very little expense. A partnership can generally bring together many more resources than a proprietorship because of the increase in the number of people involved. These added resources are not only financial in nature; the business also benefits from the variety of unique talents that many different individuals can bring to it.

- The biggest disadvantage of the partnership is
  - The unlimited liability of each general partner.
  - Another disadvantage is the lack of continuity and stability of a partnership.
  - When a partner leaves the partnership as a result of withdrawal, death, or incapacity, a new partnership must be formed. The old partner’s share must be liquidated, and this can often place a severe burden on the partnership’s capital position.

The corporation

- A **corporation** is a special legal entity endowed by law with the powers, rights, liabilities, and duties of a person (in fact a corporation is sometimes referred to as an “artificial” person). The corporate form of business organization typically facilitates the accumulation of greater amounts of capital when compared to proprietorships and partnerships.

- Most corporations are formed for profit-making purposes; however, there are thousands of nonprofit corporations in existence. These **nonprofit corporations** embrace many areas of activity, including those of religious, governmental, labor, and charitable organizations.

Stock of the corporation

- When corporations are formed, shares of stock are sold to those who are interested in investing and risking their money in the enterprise. A share of **stock** is a piece of paper, in prescribed legal form, which represents each person's amount of ownership in the corporation.

- **Common stock** normally carries the privilege of voting for the board of directors that oversees the activities of the corporation. **Preferred stock** differs from common stock in that it is usually nonvoting, and has a preferred position in receiving dividends and in redemption in the case of liquidation. Thus, voting rights are exchanged for lower risk on the investment of capital in the corporation.

Stock of the corporation

- Thus, there are two specific types of stockholders in a for-profit corporation. Common stockholders are willing to take risk. They invest in the corporation typically because they believe the value of their stock will increase over time. At the annual meeting, common stockholders are the ones that vote for the board of directors of the corporation. Each common stockholder has one vote per share of common stock.

- In contrast, preferred stockholders tend to take less risk on their investment in the corporation. The price of preferred stock typically fluctuates less than common stock in publicly traded corporations. Also, preferred stockholders often invest for the dividends granted by the corporation.

The corporation

- The primary advantage of the corporate form of business organization is that the **stockholders** (owners) are not personally liable for the debts of the organization, and in most cases are not responsible for the liability that occurs through the corporation's business activities. The assets of the corporation are all that are at risk in settling most claims.

- Transfer of ownership is also easier in a corporation than in other business forms. Usually, a stockholder can sell shares of stock to anyone for any price that the buyer is willing to pay. Because corporations' ownership rights are traded freely, it is relatively easy for them to raise large amounts of equity capital. Finally, the corporation is perpetual in nature. Death, withdrawal, or retirement of its shareholders has little effect on the life of the corporation

Cooperatives

- Owned, operated and controlled by members, a **cooperative** is a distinct form of the corporate form of business. Cooperatives are committed to helping members improve the prices they receive for the products they produce and/or reduce the prices paid for the inputs necessary to grow those products.
- Cooperatives also exist to help members find markets, and/or improve the negotiating position of members. Cooperatives provide economic and/or operational benefits to member-owners, and then return the profit to the member-owners based on each member's use of the cooperative.

Cooperatives

- Three specific features delineate cooperatives from non-cooperative businesses:
  - Member owned, member controlled (A fundamental principle undergirding cooperatives is that they must be owned and controlled by the people who conduct business with them.)
  - Operation at cost (In most cases, a cooperative’s net income is distributed to individual members in proportion to the volume of business that they have done with the cooperative.)
  - Limited returns on capital (Limiting returns on member equity to a nominal amount helps to ensure that members holding stock in the cooperative are not tempted to view the cooperative as an investment in and of itself, but rather as a service to their own business.)

Strategic alliances

- Many agribusinesses have formed **strategic alliances** and related cooperative relationships with other firms. Strategic alliances are cooperative agreements between firms that go beyond normal firm-to-firm dealings, but fall short of being a merger or full partnership and ownership. Such alliances can include joint research efforts, technology-sharing agreements, joint use of production facilities, agreements to market each other's products and the like.

- There are several advantages to firms that form strategic alliances.
  - First, firms can collaborate on technology or the development of new products.
  - Second, firms can improve supply chain efficiency by working together.
  - Third, firms can gain economies of scale in production and/or marketing.