Montana
Father-Son Business Agreement
For Farm or Ranch

By H. R. STUCKY and LAYTON S. THOMPSON
CONTENTS

MERITS OF FATHER-SON AGREEMENT ........................................... 3
   The Farm Stays in the Family ............................................. 3
   Advantages to Father and Son ............................................ 4

THE SON SHOULD GROW INTO THE BUSINESS ................................ 5
   An Early Beginning is Desirable ........................................ 5
   The Agreement Should Provide for Change ................................ 8
   Credit, Wisely Used, Can Help ........................................... 8

ELEMENTS OF A SUCCESSFUL AGREEMENT .................................. 9
   Make Room for the Son ..................................................... 9
   Provide a Separate House for Each Family ............................. 9
   Make an Effort to Get Along Together ................................ 10
   Keep a Good Set of Farm Records ...................................... 12
   Put the Agreement in Writing ........................................... 13

SUGGESTIONS FOR PREPARING THE AGREEMENT ............................. 18

THE AGREEMENT FORM .......................................................... 24
Montana

Father-Son Business Agreement
For Farm or Ranch

By 

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Merits of Father-Son Business Agreement

The Farm Stays in The Family

The smooth transfer of farms from one generation to the next with the greatest benefit or least inconvenience, both to retiring and to beginning farmers, is a problem of increasing importance in Montana. When there is a desire to keep the home farm in the family, the problem is complicated by the fact that many fathers are not ready to retire by the time a son interested in farming reaches maturity and is anxious to get started.

In this circular a method is discussed whereby a father can interest the son in the farm business and permit him to share in it. Although the proposed arrangement is called Father-Son Agreement, it can be applied equally well to an arrangement between a farmer and his son-in-law, two or more sons, a daughter, or any non-related young farmer with whom he feels he can work.

The question of who is to take over the farm when the father retires is considered important enough by many people to justify considerable thought and effort in working out the proper arrangement. It is inevitable that someone will eventually take over, and much can be said for any arrangement which will keep on the farm some of the best young people of the rural community. Such an arrangement must, above all, keep the young people interested in farming.

There is no use encouraging a son to farm if he does not like

*It is customary in Montana to make a distinction between the terms “farm” and ranch.” However, for the sake of simplicity, in this bulletin the term “farm” is used to mean “farm” or “ranch.” Also, reference is made throughout the bulletin to father and son agreements. The terms should be understood to include the mother and the son’s wife, as the bulletin describes a family agreement.
to farm. Also, the son’s wife should like farm life. Farming is an occupation in which every member of the family has a responsibility, and it is as important that the young people be willing to accept that responsibility as it is that the parents be willing to grant it. There is no substitute for the kind of interest which makes proper care of livestock, machinery, buildings, fences, and soil, a pleasure rather than a burden.

It is a fine thing when a son can begin farming early, grow into the farm business, and eventually become the owner. Many farm folk desire to keep the farm in the family, and it is often best for a young man to start farming in the home community and on the home farm. He knows the people, the soil, the farming methods, and the farm problems peculiar to the home community.

The community gains when father-son arrangements result in keeping the farm units productive and in the hands of people who have an interest in the community and are loyal to it because they expect to make their homes there. Many improvements such as good roads, electricity, good community organizations, and good marketing facilities depend to no small degree on keeping the young people interested in the land. Although farm life is often hard work, much of the dullness and drudgery has been or can be removed from farming by the use of modern farm machinery, by equipping the home with modern conveniences, and by developing the right kind of community life.

Advantages

From the standpoint of the parents, several advantages flow from helping the son grow into the farm business. Such an arrangement will allow the older persons to “slow down” as time goes on without giving up the farm and without causing a decrease in its productivity. The father can gradually ease up on the more strenuous work and devote more time to management and perhaps to community affairs. In some cases he may even go into a public office, a business venture, or some other side line. A very important requirement for success in “father-son” or other such arrangement is that the older persons be able and willing gradually to turn over a measure of responsibility and control to the younger persons as their ability and contribution to the business increases.

“On the farm retirement” for the father and mother is made possible if two houses can be provided. In some cases, at least, this is desirable. It costs less to retire on the farm, and retirement can come earlier than if the older folk wait until they can afford to move to town. With better roads and more modern conveniences in farm homes, they can enjoy most of the comforts
and pleasures they might have by moving to town, without break­
ing the ties with neighbors and friends or leaving the land they
love.

The son also receives definite benefits. If a young man
wants to farm, he finds it much more difficult to get started now
than it was a generation ago. The increase in the amount of ma­chinery and equipment required involves a much greater invest­ment than was formerly necessary. Partly because of the in­creased use of machinery, the average size of Montana farms has
increased and consequently the number of farms has decreased,
making fewer farms available for new operators. The mechanized,
commercialized farms call for more capital, more experience, and
more training than the smaller, less mechanized units of the past.

The time required for a young man to save sufficient capital
and acquire sufficient experience to operate in competition with
established farmers often is so great that he loses his incentive
to farm. A son who can acquire capital and experience earlier
by operating with his father may be very fortunate. It can
shorten the period required for him to get started. It can lead
to early assumption of full responsibility. Many farmers spend
the best years of their lives at the hardest kind of labor before
they have enough capital to apply their labor productively.

The Son Should Grow Into The Business

An Early Beginning is Desirable

Through a father-son agreement the son can
begin early to have some part in the farm busi­ness, and his share of the responsibility and of
the income, too, can increase as his ability and
his financial contribution increase. An early beginning will stimu­late his interest in farming and will enable him to tie in his training
in school with firsthand experience. If the son dislikes farming,
or if the temperament of the son or his father is such that they do
not work well together, the sooner they find it out the better.

It is usually too late to begin an agreement when the father
is ready to retire because by then the son will probably have es­
tablished himself someplace else, on another farm, in business,
or in a profession, and will no longer be interested in the home
farm, or cannot afford to make the shift.

This bulletin describes a father and son agreement which
will cover the entire farm or ranch business. The son can, of
course, obtain some farm experience before he is old enough and
mature enough to think about and work on the whole spread.
Many farm boys get their first active participation through some
4-H Club or Future Farmer projects such as raising of a calf, pig, lamb, pen of poultry, or acre of crop. This is a good way to combine education with experience and to stimulate interest in farming. As a result of the project the boy may at first have a part in only one enterprise. The sooner he can be given some interest in the entire farm, however, the better it will be. He is encouraged to think in terms of all, rather than part of the business. This is a good thing for the farm and provides more general experience for the son. It will hasten the decision as to whether or not the boy wants to farm and whether or not he and his father can work together.

This does not mean that specialization is never desirable. Oftentimes it works well when different members of the family have the chief responsibility for specific enterprises. This may be especially true if there are two or more sons or daughters included in the farm agreement. One member of the family might have chief responsibility for the dairy enterprise, another for poultry, another for crops, and so on. It would be better, even then, for all to share in the whole farm income on a basis of the contribution of each to the total farm business. This will make the accounting much more simple, the income of each member less variable, and the interest of all in the whole business more certain.

When the son has begun early with a 4-H Club project, he is likely to develop a desire to study agriculture in high school and later to take the College short course or the regular four-year College course. The father-son agreement could encourage a young man to get this education by increasing his interest in agriculture, and also by furnishing him agricultural employment during the summer where he could earn much of the money necessary for his education. This business agreement also gives him an opportunity to return to the farm after completing his education. Many well-trained capable young men do not go into farming or ranching after completing their education because they do not have a farm deal worked out in advance. Also many young farmers who would like to get some additional education may be enabled to do so if an agreement is in effect, thus caring for the management of the farm unit during the time they would need to be away.

An Early Beginning is Desirable—Through a father-son agreement the son can begin early to be interested in the farm business. The pictures on the opposite page suggest progress by starting with a small beginning, and by successive steps earning an interest in the entire farm business.
Flexibility is a desirable characteristic in a father-son agreement. The son should be encouraged to increase his contribution of management and capital each year, if possible; the type of agreement described in this bulletin allows him to do so. Gradually he will take most of the traditional steps up the agricultural ladder though they will be taken on the home farm with his father's help. At first his chief contribution will be labor, but he will soon be able to supply some of the working capital. This gives him an opportunity to increase his income by investing his savings in the business. Also, it is usually easier to save in the form of increased inventory than in the form of cash. Later he may reach the stage of full ownership of the working capital as the father retires, with perhaps some arrangement whereby he can begin to obtain an equity in the real estate.

Two changes in the farm business may occur as the son increases his investment. One is that the farm business may grow larger, either by adding acreage to the farm or by adding capital in the form of livestock or equipment. The other possibility is that the father's investment in the working capital or real estate may decrease as the son's investment increases. It may be that the father will consider his investment in the farm business as his provision for old age and will want to withdraw it gradually to provide himself and his wife with a comfortable living as fast as the son can replace it with capital of his own, or the father might gradually withdraw his capital from the farm and invest it elsewhere.

Any young man who enters into an agreement with his father, father-in-law, or with some neighbor, hopes eventually to gain a working interest in the productive livestock and machinery, and eventually in the real estate. In order to gain this financial interest in the business, he should establish a good credit rating in his community and learn to make wise use of credit.

Credit is a very valuable asset to a young farmer if he learns to make proper use of it. Many farmers fail because they recklessly borrow money or do not follow a sound plan for repayment of these obligations. Many young farmers also fail because they are "timid" in the use of credit, and as a result do not operate efficiently due to lack of adequate livestock or machinery. When a farmer, after a thorough investigation of the probable market for the product he will produce, finds a place in his operation where he might borrow money to buy productive livestock or productive equipment and repay the loan, he should not hesitate.
to borrow a reasonable part of the money for such purposes (possibly 50% to 75%). Ordinarily he should avoid borrowing money for day-to-day living expenses. If he finds that he has to borrow for these things, he should review the entire farm or ranch operation to determine whether it is large enough to support the share agreement or to determine changes necessary in the operation to make it return a higher income. There are four general indications which point to good management. They are: (1) yield per acre, (2) yield per animal, (3) yield per dollar invested, and (4) return per worker. When a farm or ranch is operated efficiently so that it will rank above average for the community on three or more of these points, it will ordinarily be a successful operating unit. Credit when used wisely by the young operator getting a start in farming will likely assist in increasing his income and improving his living conditions.

Elements of a Successful Arrangement

Make
Room For
The Son
Provide a
Separate
House For
Each Family

A father-son arrangement is bound to fail unless the farm business is large enough eventually to provide satisfactory income for two families. The business may already be of sufficient size and the son only replaces the labor previously hired. If not, there are numerous ways of expanding. It may be possible to rent or buy more land, and often the extra land can be farmed with little or no additional equipment. Or in some parts of Montana the business may be enlarged by an increase in the acreage of crops requiring additional labor and capital, such as sugar beets or canning crops, or by adding livestock enterprises such as dairying, poultry enterprise, or livestock feeding. Additional income may be obtained from custom work. Occasionally one of the parties may engage in a business or obtain income from a public office or other off-the-farm employment. Also, additional income may be obtained by use of more efficient farming operations and by the use of fertilizer and soil conservation practices.

Not only must the business be of sufficient size, but also there should be a separate house for each family if the son is married. This is an essential if any two families are to get along, and it can be even more important when the families are related. It is even better if the houses are not in the same yard, but are separated by as much as a quarter or a half mile. Some farms are equipped with two homes. If there is only one house, additional housing may be obtained by buying or leasing a nearby farm with a house on it. It may pay to build a second house on the farm especially if the parents expect to re-
A separate house for each family is an essential.

tire on the farm. Until the son is married, of course, he might very well board with his father and mother.

Another essential is that the father and son must get along together. The son needs to recognize the value of the experience and more mature judgment of the father, and the father must appreciate that the son is eager to take on responsibilities, to “try his wings.” Each should be willing to try new ideas and each must occasionally be able to yield to the other’s point of view. There are cases where the temperament or attitude of the father or son or other members of the family is such that there is no chance of a father-son business agreement working. Difficulty of this kind, however, need not occur. Much of the friction which takes place arises out of misunderstanding and
can be avoided if the agreement is carefully worked out in detail and put in writing, and if a good set of farm records is kept.

If there are several sons or daughters in the family, it makes a difference. Usually not more than one son or daughter, or at the most two, will wish to enter into the farming agreement. Farms are few in number that will provide sufficient income for more than two or at most three families. Also, the other sons or daughters will likely find other work which is more attractive to them. A father-son agreement should be fair to all members of the family. As was stated above, the form of agreement recommended in this circular can be used when more than one son is interested in the farm business, but only in a few cases will it be advisable to enter into a multiple agreement except on a temporary basis.

No father-son agreement should be entered into without the knowledge of all members of the family and each member of the family should be informed when any major change is made.
Whenever the son or sons who stay on the farm make improvements on the farm which add to its value, or whenever they make an important contribution toward the living expenses of the parents, they should be given credit for these items in any settlement of the estate. Provision for this should be made in the written father-son business agreement.

Keep a Good A good set of farm accounts is a must. It Set Of is good experience for the son to keep the accounts, at first under the supervision of the Farm Records father. As a minimum, these accounts should include: (1) a beginning and ending inventory of all real estate and personal property, showing the investment of each party, (2) a record of all cash receipts and of all cash expenditures, (3) a record of all cash advanced to each party and of all cash outlays made by either party from his own funds toward current expenses. The farm record is more than useful—it is essential for making out income tax returns, for guidance in improving the farm business, and for making settlements and prorating the
shares of net income. There is much less likelihood of misunderstanding if all the items listed above are carefully recorded. The *Montana Farm and Ranch Record Book* is useful for this purpose.

**Put The Agreement In Writing**

Finally, a written agreement is a necessity for several good reasons. In the first place, the agreement is apt to be more carefully considered if it is put in writing, the terms stated with precision, and a clear understanding obtained concerning the rights and responsibilities of each party. In the second place, memories are notoriously short and people forget what conclusions were reached, especially the details. Each party having a copy of the agreement reduces misunderstanding over what was agreed to. In the third place, a written agreement is necessary for the protection of either party in the case of death of the other. Also, the agreement serves as protection for the heirs of the deceased party. This protection is especially important when property which is to be improved during the life of the agreement will later be inherited by the son and other heirs.

**The Agreement**

The father-son agreement described in this bulletin works on the general principle that each party shall share in the annual gross farm returns in proportion to his total annual contribution of labor, invested capital, and cash. The father will usually make the total contribution of owned real estate at the beginning of the agreement. The value of this contribution will be measured by applying an agreed interest rate to the normal value of the land.

The labor contribution of the father and son should be based on the long-time average wage for hired farm workers, although there will be considerable variation according to the age, health, or general ability of each party. It should not be overlooked that the father, because of his experience, knowledge of the business, and skill in doing the work should be credited with a larger wage, at least at the start. The wage may be paid monthly throughout the year to either or both parties, or only used to figure the labor contribution each makes, the current needs of each party being taken care of by advances whenever cash is needed. The policy on this matter must be clearly understood by each party.

Contributions of machinery, equipment, and livestock (ex-
cepting feeder livestock) will also be measured by applying an agreed rate of interest to a reasonable valuation of the livestock, machinery, and equipment supplied by each. The son should begin early to make some contribution in addition to his labor.

A large investment in machinery and equipment is required in Montana under the present system of mechanized farms and with the increased average size of farm units.

Contributions each party makes toward current expenses, such as taxes, seed, tractor fuel, feeder stock, or feed will be counted in full amount in computing the percentage of gross income going to each party. It is a good thing for the son to make some contribution to the business by supplying part of the current expenses, for in this way he can increase his share of the net farm income. The parties should be in full agreement on this matter and an estimate of the probable contribution to be made by each should be made at the beginning of each year. When bank credit is used for farm expenses, the son might take a part or all of the responsibility for repayment and be given credit for this contribution.
Drawing up The First Agreement

In drawing up the first agreement for the farm or ranch, start by listing the items of operating expense on a blank sheet of paper. The land, machinery, and livestock will be listed first. Following this will come the current expenses such as hired labor, seed, tractor fuel, oil, and other items. After all of the expense items have been listed, indicate opposite each item the percentage which will be contributed by the father in one column and the percentage to be contributed by the son in a second column.

For example: The father may agree to furnish all of the land and buildings, all of the machinery, and three-fourths of the productive livestock. He may also plan to pay two-thirds of the cost of hired labor and one-half of the tractor fuel and oil. These would be listed as follows:

<table>
<thead>
<tr>
<th>Item</th>
<th>Father</th>
<th>Son</th>
</tr>
</thead>
<tbody>
<tr>
<td>Land and buildings</td>
<td>100%</td>
<td></td>
</tr>
<tr>
<td>Machinery</td>
<td>100%</td>
<td></td>
</tr>
<tr>
<td>Productive livestock</td>
<td>75%</td>
<td>25%</td>
</tr>
<tr>
<td>Hired labor</td>
<td>67%</td>
<td>33%</td>
</tr>
<tr>
<td>Tractor fuel and oil</td>
<td>50%</td>
<td>50%</td>
</tr>
</tbody>
</table>

All other expense items would be listed in a manner similar to the above example. The percentage indicated for each item will vary, depending on the experience and the financial ability of the son. These percentages will also vary depending on whether the father expects to continue as an active operator of the farm or ranch with the son, or whether he desires to retire gradually during the next few years and have the son eventually take over full management.

The next step in making up the agreement and estimating the shares to the father and to the son is to estimate and list the annual expense of operating the farm or ranch on a form similar to that on the following page.
TABLE I

Example of the Method for Estimating Income Shares For All Types Of Father-Son Farm or Ranch Business Agreements

<table>
<thead>
<tr>
<th>Item</th>
<th>Estimated Total Value (A)</th>
<th>Estimated Interest Rate (B)</th>
<th>Estimated annual cost</th>
<th>Whole Farm Share (C)</th>
<th>Father's Share (D)</th>
<th>Son's Share (E)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Dollars</td>
<td>Percent</td>
<td>Dollars</td>
<td>Dollars</td>
<td>Dollars</td>
<td>Dollars</td>
</tr>
<tr>
<td>INVESTMENT EXPENSES:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Land and buildings</td>
<td>28,000</td>
<td>4</td>
<td>1,120.00</td>
<td>1,120.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Tractor and work stock</td>
<td>2,350</td>
<td>5</td>
<td>117.50</td>
<td>117.50</td>
<td></td>
<td></td>
</tr>
<tr>
<td>3. Productive livestock</td>
<td>5,550</td>
<td>5</td>
<td>277.50</td>
<td>190.00</td>
<td>87.50</td>
<td></td>
</tr>
<tr>
<td>4. Machinery and equipment</td>
<td>3,400</td>
<td>5</td>
<td>170.00</td>
<td>120.00</td>
<td>50.00</td>
<td></td>
</tr>
<tr>
<td>5. Feed and supplies</td>
<td>400</td>
<td>5</td>
<td>20.00</td>
<td>20.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>6. TOTAL INVESTMENT EXPENSE</td>
<td>39,700</td>
<td></td>
<td>1,705.00</td>
<td>1,567.50</td>
<td>137.50</td>
<td></td>
</tr>
<tr>
<td>CURRENT FARM EXPENSES:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>7. Labor:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. Son</td>
<td></td>
<td></td>
<td>1,200.00</td>
<td>1,200.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>b. Father</td>
<td></td>
<td></td>
<td>1,200.00</td>
<td>1,200.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>c. Unpaid family</td>
<td></td>
<td></td>
<td>300.00</td>
<td>300.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>d. Hired</td>
<td></td>
<td></td>
<td>460.00</td>
<td>230.00</td>
<td>230.00</td>
<td></td>
</tr>
<tr>
<td>8. Repairs:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. Building</td>
<td></td>
<td></td>
<td>62.00</td>
<td>31.00</td>
<td>31.00</td>
<td></td>
</tr>
<tr>
<td>b. Fence</td>
<td></td>
<td></td>
<td>100.00</td>
<td>50.00</td>
<td>50.00</td>
<td></td>
</tr>
<tr>
<td>c. Machinery</td>
<td></td>
<td></td>
<td>243.00</td>
<td>178.00</td>
<td>70.00</td>
<td></td>
</tr>
<tr>
<td>9. Depreciation:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. Building and fences</td>
<td></td>
<td></td>
<td>100.00</td>
<td>100.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>b. Livestock</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>c. Tractor and work stock</td>
<td></td>
<td></td>
<td>128.00</td>
<td>128.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. Land and buildings</td>
<td></td>
<td></td>
<td>200.00</td>
<td>200.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>d. Machinery</td>
<td></td>
<td></td>
<td>580.00</td>
<td>405.00</td>
<td>175.00</td>
<td></td>
</tr>
<tr>
<td>10. Tractor fuel and oil</td>
<td></td>
<td></td>
<td>450.00</td>
<td>225.00</td>
<td>225.00</td>
<td></td>
</tr>
<tr>
<td>11. Machine work hired</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>12. Veterinary charges, livestock expense, replacements</td>
<td></td>
<td></td>
<td>112.00</td>
<td>77.00</td>
<td>35.00</td>
<td></td>
</tr>
<tr>
<td>13. Feed</td>
<td></td>
<td></td>
<td>72.00</td>
<td>50.00</td>
<td>22.00</td>
<td></td>
</tr>
<tr>
<td>14 Seed: Hay and permanent pasture</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. Grain crops</td>
<td></td>
<td></td>
<td>75.00</td>
<td>50.00</td>
<td>25.00</td>
<td></td>
</tr>
<tr>
<td>15. Commercial fertilizer</td>
<td></td>
<td></td>
<td>100.00</td>
<td>70.00</td>
<td>30.00</td>
<td></td>
</tr>
<tr>
<td>16. Water charges</td>
<td></td>
<td></td>
<td>230.00</td>
<td>230.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>17. Automobile and truck expense for farm use</td>
<td></td>
<td></td>
<td>215.00</td>
<td>160.00</td>
<td>55.00</td>
<td></td>
</tr>
<tr>
<td>18. Insurance:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. Buildings</td>
<td></td>
<td></td>
<td>11.00</td>
<td>11.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>b. Personal property</td>
<td></td>
<td></td>
<td>20.00</td>
<td>15.00</td>
<td>5.00</td>
<td></td>
</tr>
<tr>
<td>19. Taxes:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. Personal property</td>
<td></td>
<td></td>
<td>80.00</td>
<td>50.00</td>
<td>30.00</td>
<td></td>
</tr>
<tr>
<td>20. Miscellaneous (including cash rent)</td>
<td></td>
<td></td>
<td>122.00</td>
<td>61.00</td>
<td>61.00</td>
<td></td>
</tr>
<tr>
<td>21. TOTAL CURRENT FARM EXPENSES</td>
<td></td>
<td></td>
<td>6,250.00</td>
<td>3,705.00</td>
<td>2,544.00</td>
<td></td>
</tr>
<tr>
<td>22. TOTAL INVESTMENT AND CURRENT FARM EXPENSES (line 7 plus line 22</td>
<td></td>
<td></td>
<td>7,956.00</td>
<td>5,275.50</td>
<td>2,681.50</td>
<td></td>
</tr>
<tr>
<td>23. Approximate percentage of total contributed by each party</td>
<td></td>
<td>100%</td>
<td>66%</td>
<td>34%</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Note: (1) The form used here was recommended by the U. S. Bureau of Agricultural Economics in Cooperation with the Extension Service in Circular DS-27. (2) The cost figures and the division between the father and son were derived from Montana records.
How Will Annual Costs Be Estimated

The annual investment expense is calculated by taking the long-time earning capacity value of the land and multiplying this value by the prevailing interest rate on real estate mortgages. For example, suppose the land and buildings are valued according to the long-time earning capacity at $25,000 and the interest rate for land is figured at four percent, then the annual charge for the use of this land would be $1,000 ($25,000 value of the land and buildings, times four percent interest rate, equals $1,000). The investment charge for the productive livestock, machinery, and equipment would be calculated in the same manner, using average prices for the machinery and for the productive livestock. The interest rate usually should be the prevailing production credit interest rate which is higher than the interest on real estate mortgages because of the larger risks of loss involved.

The depreciation charges will be the same as the depreciation charges set up in the income tax records for the farm. These average values, interest rates, and the annual investment expenses are listed in Table 1, Columns A, B, and C on Page 16.

The cash expenses can be estimated, but it is preferable to take them from the farm and ranch record book for the past year. A few adjustments may be made from the past year's record if major changes are being made in the plan for operating the farm under the father-son agreement.

After the investment expenses, cash operating expenses, and depreciation charges have been listed in Table 1, Column C, these costs should then be divided between the father and son and listed in Columns D and E. The division will be made on the basis of the proportion of these expenses to be furnished by the father and the son as already agreed to (as suggested on Page 15).

Next, add up the expenses as listed in Columns C, D, and E. Then determine what percentage of the total (shown on line 22, Column C) is to be furnished by the father (line 22, Column D) and the son (line 22, Column E). The percentages are then written on line 23.

The most fair way of dividing the farm or ranch income is on the value of the total contribution made by the father and the son for the year. Therefore, the percentages shown on line 23, Columns D and E are roughly the share of the income which should go to each.

Is The Agreement Satisfactory? The father and son now can determine whether the shares as worked out are workable and satisfactory. Are the amounts required within the financial means and within the abilities of each party? Will the incomes resulting for each be suf-
ficient to support the families dependent upon them? If found to be satisfactory on these counts, they then can be entered in the agreement as the contribution each plans to make to the business. There are four sections in which these figures will be entered.

1. Investment percentages contributed by each will be entered into the agreement in Section 4.

2. Current farm expense percentages are entered in Section 5.

3. The estimated long-time average value of the land and buildings and a reasonable value for the productive livestock are entered in Section 9, showing the dollar value contributed by the father and son. By applying a reasonable interest to these values the annual investment charge will be determined.

4. The months of labor, the rate per month, and the total annual allowance for the father and the son’s labor will be entered in Section 10.

Make Income Estimates Annually

It is desirable that an estimate similar to the above example be worked out at the beginning of each year for several reasons:

1. The estimate will give each party an idea of the size of his probable share for the year.

2. The father and son will list the items of cost which each can furnish. This gives each an opportunity to agree on the items of cost which he will contribute.

3. The increasing ability of the son to contribute both in experience and in capital can be reflected in the changes made in their contributions each year.

Suggestions for Preparing The Montana Father-Son Agreement for Farm or Ranch

This set of instructions has been prepared to point out some of the factors to consider in preparing each section of the agreement. The numbers and headings below correspond to the numbers and headings on each section of the agreement form.

GENERAL—The Montana Father-Son Farm or Ranch Business Agreement form includes clauses covering most of the important points which should be considered in preparing such an agreement. Clauses in the agreement which do not apply can be marked out. Other clauses to cover special considerations may be added in the spaces provided. The best date for the agreement to begin will usually be when inventories of crops, feed, and supplies are lowest. In many cases this date will correspond with the time of taking
the January 1 inventory. However, the agreement can be started at any time during the year.

1. DESCRIPTION OF LAND: The legal description should be complete, including a description of water rights. In some cases the most convenient method of describing a farm or ranch is by use of a township plat on which the location of all owned land or leased land can be shown.

2. TERM: This section is worded so that the agreement is automatically renewed from year to year unless written notice is given a specified number of days before the annual expiration date. Not less than 60 days notice should be given, and preferably notice should be given six months before the expiration date.

3. LIMITATIONS OF COMMITMENT: This limitation is to prevent either the father or the son from making unlimited sales, purchases, or contracts without the consent of the other party except as provided in Section 8 of the agreement.

4. INVESTMENTS: All machinery, livestock, and equipment should be inventoried at the beginning of the agreement, and each year thereafter. An inventory is necessary for determining the gross income of the business and also for determining the contribution being made by each party. The investment contributed by the father and the son will change as the son's participation in the business increases.

The first inventory, when starting the agreement, should use normal or reasonable prices for arriving at inventory values of the land, productive livestock, and machinery contributed by each. Inventories made each year thereafter should use these same prices less depreciation for the items of the original inventory still carried on the record. New purchases added to the original inventory will be entered at cost. The original inventory and the valuation of the livestock produced on the farm should not be changed to reflect fluctuations in current prices.

5. CURRENT FARM EXPENSES: The percentage of each expense item to be contributed by the father and the son should be indicated following each of the items listed in this section. The purpose here is to provide for an understanding as to the contribution each person expects to make toward the operating expenses. The actual contributions, which may vary somewhat from this plan, will be carefully recorded and used as the basis of sharing the income (see Section 6). The father and the son may not pay the exact percentages on each item as indicated in the plan, but the total contribution made by each person should be very close to that indicated in the plan.
The common practice is for the son gradually to increase his total contribution to the farm operating expenses as he gains experience and financial ability. The amount of the increase which the son can be permitted to make must be agreed upon by the father and son and will depend on the size of the total farm unit and the retirement plans of the father.

6. DIVISION OF INCOME: Gross income for each year consists of the sales of crops or livestock which were produced on the farm or ranch during the year plus any crops or livestock produced during the year which have not been sold and are on hand at the end of the year. The gross income is to be divided between the father and son on the basis of the percentage of total cost furnished by each. The total costs will consist of (1) farm expenses taken from the farm account book, (2) investment charges taken from Section 9 of the agreement, and (3) labor charges taken from Section 10.

Which Expense Claims Come First? If the farm or ranch income takes care of all expenses and leaves a net income, there is no problem of which expense claim will be paid first. If the gross income should fall short of all claims in any one year, due to hail, drought, or some other cause, it is best to have an understanding on how the income will be divided. The usual practice in settling claims is first to pay all the creditors’ claims for annual operating expenses.* After the claims to creditors have been paid, each party should be repaid for any cash outlay he may have made toward the operating expenses for the year. Next in order will be the wage claims of the father and son. In bad years it may not be possible to pay the full wage allowance from farm income. Only after the total current expenses and the wage claims of both parties have been paid should the interest charge on the land, livestock, and machinery investment of each party be taken care of. Any shortages should be shared proportionately between the father and son.

7. INCREASE IN INVENTORY: In making the annual inventory, a careful separation should be made between those increases in inventory which resulted from production under the agreement and those which resulted from purchases by either the father or the son and were paid for from his own funds.

*In some cases the annual interest charge which must be paid by either or both parties on real estate mortgages and on production credit loans is counted as a farm expense. Only the interest on the father’s and son’s equity will then be deferred until after all other creditor claims and wage claims are paid. Depreciation charges on buildings, equipment, and livestock will have a similar claim against the annual cash income as the interest on the father’s and son’s equity in the invested capital.
Inventory increases from livestock and crops produced on the farm or ranch or that were purchased from money earned jointly under the agreement are a part of the joint income for the year. This income is subject to division between the father and son on the percentage of contribution basis, just as cash from sales would be divided.

Inventory increases which are the result of purchases by the father or the son and that have been paid for from the personal cash of one or the other would be listed in the inventory as being owned by the individual who purchased and paid for the item. These items are not a part of the joint income and ownership, and for this reason are not subject to division between the parties. These purchases should be made only in accordance with Section 8 of the agreement.

8. SALES AND PURCHASES: Sales or purchases of major items should be agreed to by the father and son before these transfers are completed. Numerous sales of milk and eggs may be made in small lots throughout the year. The marketing place and the quality of produce to be marketed should be discussed. Purchases of livestock, machinery, or land will require consideration of price, financing, and determination of need for the purchase in the farm or ranch operation. Sales will involve a decision on which stock, machinery, or land will be sold, the consideration of price, time of delivery, and the effect of the sale on the farm or ranch operation. These purchases or sales should be considered well in advance of the transaction, if possible.

9. LAND, LIVESTOCK, EQUIPMENT VALUATION: The value of the land, tractor and work stock, machinery and equipment, and productive livestock are listed in this section. Shown also is the amount of the investment in each of these items furnished by the father and by the son. The value of the land should be based on its long-time productive capacity. The value of the other items should be placed on about prewar average values to prevent setting up an inflating investment charge. The interest rate used for land should be the rate commonly used for farm mortgages. The interest rate for the livestock and machinery should be the common production credit rate.

The values placed on the investments should not be changed from year to year to reflect current fluctuations in prices. The total investment contribution will change only as major purchases are made or when there is a major change in the amount of investment contributed by the father or the son.

10. LABOR CONTRIBUTION OF FATHER AND SON: The agreed monthly wage and the number of months the father or
son expects to work on the farm is a measure of the labor contribution of each party. For example, a father working with one or more young sons may put in twelve months of work and be allowed a higher labor wage per month than the relatively immature and inexperienced sons who may still be in school. These young fellows may put in only the summer months on full time. In another example, the father may wish to be practically retired and turn over the work and management to a mature and experienced son. In this case the son may put in twelve months on the farm while the retiring father may put in only a few months during the busy season.

It is not necessary that this monthly wage be paid each month, but it must be considered in the annual settlement of the accounts. This monthly wage is desirable from the son’s standpoint as it allows him an amount which he can use for clothes, groceries, if he is maintaining his own home, and some spending money. He may wish to draw only a part of this allowance and leave the balance in the business to increase his ownership in livestock or machinery, or to increase his contribution to the operation of the farm.

Whatever is to be the policy, it should be a matter of definite understanding and entered into Section 10 of the lease. There should be balance between the values established for investments (Section 9) and the monthly rate for wages (Section 10.) For example, if the land is entered at inflated values then the wage rate should be set on the same basis. It is much more desirable that the investment values and wage rates be established on a conservative basis.

11. RECORDS: The records should show (1) all expenses and receipts, (2) a complete beginning and ending inventory showing the investment of each party, and (3) all wage allowances made to either party and all cash outlays made by either party toward current farm expenses. It is desirable that a standard record book be secured and that the same type of book be kept from year to year. This will provide a record which will be more easily kept due to both parties being familiar with the system. It will also provide a uniform record which can be used for adjustment of losses and gains between years when making income tax returns. The Montana Farm and Ranch Record Book is an example of such a standard record book. These are available through the County Agricultural Agent’s offices in Montana at low cost.

12. RANCH OPERATIONS:
A, B. and C are self explanatory.
D. Provisions for livestock may include such items as
13. SOIL CONSERVATION:
A. Examples might be the proper use of irrigation water or stocking of the range in accordance with its carrying capacity.
B. The use of the manure will vary with type of farming.
C. Straw, stubble, and crop residue should be conserved in accordance with the accepted practices.
D. Fertilizer may be of benefit for two or three crop years. In case of termination of the agreement, the father should agree to pay a larger share according to his expected future benefits.
E. Care should be taken to set up the weed control program in accordance with successful practices in the community.

14. IMPROVEMENTS: Ordinarily improvements which add value to the farm real estate will be made by the father (owner). There is no reason why the son could not make some contribution toward such improvements, but if he does it is only fair that provision be made that other heirs do not cash in on his efforts when the estate is settled. In case he buys the farm from the other heirs at a later date, he may find himself paying for the improvements twice. As is indicated on the agreement form, the son’s interest might be protected in the form of a lien against the farm real estate.

15. LIVING ARRANGEMENTS: If possible, a house should be provided for each family. If an additional house is rented for either family, the rental cost can be shared as a farm operating expense. If either party boards the other, the amount which is to be charged for board should be agreed upon. There should be an understanding concerning the production and division of milk, butter, eggs, and other products used in the homes.


17. ARBITRATION: This provision is a valuable one in any lease. The arbitration committee will usually arrive at as good or better decision than will be obtained from the courts at much less expense and loss of time.

18. ADDITIONAL AGREEMENTS: No agreement form can take care of all the provisions needed under all conditions. Enter
here any items not sufficiently covered above.

19. The agreement should be signed by both parents and by the son and his wife, and the signatures witnessed by two disinterested parties.

Father-Son Farm or Ranch Business Agreement Forms Are Available

The following is a copy of the Montana Father-Son Farm or Ranch Business Agreement. The agreement prepared in the usual legal lease form arrangement is available through the County Agents' offices in Montana.

MONTANA FATHER-SON FARM OR RANCH BUSINESS AGREEMENT

THIS AGREEMENT is entered into this ............. day of .............., 19......, between ..........................................., the father, and ..........................................., the son.

1. DESCRIPTION OF LAND: This agreement is entered into for the purpose of operating a farm or ranch business on the following described real estate: ...........................................

...........................................

...........................................

...........................................

...........................................

in ..........................................., County, State of ........................................;

and on any other land which the father and the son may purchase or rent for farming or ranch purposes.

2. TERM: This lease shall be in effect from ............... 19......, to ............... 19......, and shall, with such written modifications as may be agreed to at the beginning of each year, continue from year to year thereafter unless terminated by written notice by either the father or the son to the other at least ............... months before the expiration date of this lease or any extension.

3. LIMITATIONS OF COMMITMENT: Neither the father nor the son shall have authority to obligate the other without written consent, except as specified in Section 8.

4. INVESTMENTS: The following investments shall be furnished by the father and son in the shares as designated in the columns at the right.
A. Land—
(1) Land covered by above description
(2) Any other land

B. All machinery, equipment, tools, and harness necessary for proper care of crops and livestock on ranch

C. Work stock

D. Productive livestock
(1) At start of agreement
(2) Purchased after inventory
(3) Produced under the terms of this lease

E. Other

5. CURRENT FARM EXPENSES: The following expenses shall be contributed by the father and the son in the shares as designated in the columns at the right.

<table>
<thead>
<tr>
<th>Item</th>
<th>Share to be furnished by Father, %</th>
<th>Share to be furnished by Son, %</th>
</tr>
</thead>
<tbody>
<tr>
<td>A. Labor:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(1) Son</td>
<td>xxx</td>
<td>xxx</td>
</tr>
<tr>
<td>(2) Father</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(3) Unpaid family labor</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(4) Hired labor</td>
<td></td>
<td></td>
</tr>
<tr>
<td>B. Repairs:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(1) Building</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(2) Fences</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(3) Machinery</td>
<td></td>
<td></td>
</tr>
<tr>
<td>C. Depreciation:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(1) Buildings</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(2) Fences</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(3) Tractor and work stock</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(4) Machinery</td>
<td></td>
<td></td>
</tr>
<tr>
<td>D. Tractor fuel and oil</td>
<td></td>
<td></td>
</tr>
<tr>
<td>E. Machine work hired</td>
<td></td>
<td></td>
</tr>
<tr>
<td>F. Veterinary charges, livestock expense, replacements</td>
<td></td>
<td></td>
</tr>
<tr>
<td>G. Feed</td>
<td></td>
<td></td>
</tr>
<tr>
<td>H. Seed: Hay and permanent pasture Grain crops</td>
<td></td>
<td></td>
</tr>
<tr>
<td>I. Commercial fertilizer</td>
<td></td>
<td></td>
</tr>
<tr>
<td>J. Water charges</td>
<td></td>
<td></td>
</tr>
<tr>
<td>K. Automobile and truck expense for farm use</td>
<td></td>
<td></td>
</tr>
<tr>
<td>L. Insurance:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(1) Buildings</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(2) Personal property</td>
<td></td>
<td></td>
</tr>
<tr>
<td>M. Taxes</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(1) Land and buildings</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(2) Personal property</td>
<td></td>
<td></td>
</tr>
<tr>
<td>N. Miscellaneous (including cash rent)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
6. DIVISION OF INCOME: Income from the farm will be divided on or before December 31 each year on the basis of the percentage of the cost furnished by the father and son for each year.

Section 5 shows the percentage of contribution which each plan to furnish. The Farm and Ranch Record Book kept for the farm or ranch shows all expenses and receipts and will be the basis for determining the total cash cost of the farm or ranch and to determine the percentage of the total which was contributed by the father and the son. The annual investment charge shall be taken from section 9 and the labor contribution charge shall be taken from section 10 of this lease. Revisions should be made at the end of any year in which major changes are made from the amount of contribution as shown in section 5, 9, or 10.

7. Increases in inventory of livestock and machinery shall be handled as follows: .................................................................

8. SALES AND PURCHASES: The time and place where farm products will be sold shall be mutually agreed upon by the father and son. No sale of farm products or purchase of farm equipment, livestock, or supplies exceeding $ ................ for any one item or $ ................ for any one months is to be made by either party before obtaining the written consent of the other. .................................................................

9. LAND, LIVESTOCK, EQUIPMENT VALUATION: The contribution of land, livestock and equipment furnished by the father and son, the estimated total value, the interest rate charged, and the estimated annual charge are agreed to at the beginning of this agreement as follows:

<table>
<thead>
<tr>
<th>Item</th>
<th>Est. total value Furnished by</th>
<th>Interest Rate</th>
<th>Annual Charge</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Father</td>
<td>Son</td>
<td>%</td>
</tr>
<tr>
<td>Land and buildings</td>
<td>$</td>
<td>$</td>
<td>%</td>
</tr>
<tr>
<td>Tractor and work stock</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Productive livestock</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Machinery and equipment</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>TOTALS</td>
<td>$</td>
<td>$</td>
<td>xxx</td>
</tr>
</tbody>
</table>

Note: An inventory is attached giving numbers, values, and ownership of all the items entered in this section. Values should be based on reasonable long-time average prices.
10. LABOR CONTRIBUTION OF FATHER AND SON: The contributions of labor per year by the father and son and the compensation rate per month for such labor is agreed to at the beginning of this agreement as follows:

<table>
<thead>
<tr>
<th>Months of labor anticipated</th>
<th>Father</th>
<th>Son</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rate per month</td>
<td>$</td>
<td>$</td>
</tr>
<tr>
<td>Total allowance for the year</td>
<td>$</td>
<td>$</td>
</tr>
</tbody>
</table>

This monthly wage need not be paid each month, but must be considered in the annual settlement.

11. The son will keep accurate records of all ranch expenses and receipts. A complete inventory of all grains, hay, livestock, and farm equipment will be made by the son and agreed upon by the son and father on or about each year. Numbers, value, and ownership of property shall be shown.

12. RANCH OPERATIONS:
A. The ranch shall be operated in an efficient and workmanlike manner according to the accepted practices in the community. Note any specific details:

B. Crops to be planted shall be mutually agreed upon before date of planting.

C. Crops grown on the ranch shall be grown primarily for feeding on the ranch, except

D. The following provisions shall apply to the livestock operation: (Attach supplemental sheet, if necessary)

13. SOIL CONSERVATION:
A. The soil shall be maintained and improved by the following practices:
B. All manure shall be spread on fields according to agreement as follows:

C. Straw, stubble, and crop residue shall be conserved as follows:

D. Application of commercial fertilizer, when applied, shall be agreed to before application and paid for as follows:

E. Diligence shall be used to prevent the spread of noxious weeds. Treatment of infestation and the cost thereof shall be handled as follows:

14. IMPROVEMENTS (Buildings, fences, ditches, flumes, headgates, wood lots, development of new land, etc.):

A. All improvements now in satisfactory condition shall be maintained under the following arrangements:

B. Improvements now in unsatisfactory condition shall be repaired under the following arrangements:

C. New improvements (if any) shall be made under the following arrangements:
Note: Buildings, fences, irrigation developments and other improvements added to the land owned by the father ordinarily will be done by money and labor furnished by the father.

Any money and labor contributed by the son in the construction of new buildings, fences, irrigation developments or other improvements on the land owned by the father should be recorded in a lien in favor of the son. This will protect the son's investment in the land in case this agreement is terminated or in case of a settlement of the estate.

15. LIVING ARRANGEMENTS:
A. The father shall have the following living accommodations and arrangements on the farm: .................................................................

B. The son shall have the following living accommodations and arrangements on the farm: .................................................................

16. DIVISION OF PROPERTY AT TERMINATION OF AGREEMENT: If this agreement is to be terminated:
A. The son will surrender peaceably, possession and occupancy of the premises at the termination of the lease.
B. The son shall be compensated for any permanent improvements added to the farm to which he has contributed labor or capital.
C. All property owned in common should be appraised jointly by the father and the son and conservative values established. If actual division of the property is not possible or desirable, the father agrees to buy the son’s share or to sell his own share at the appraised value.
D. The interest of the father and the son in the livestock, machinery, and equipment will be established in each annual inventory. This is necessary, as the purchase of livestock, machinery, and equipment is included as a cash farm expense, and all sales are included in the cash farm income, unless otherwise specifically agreed and so entered in the farm record books.

17. ARBITRATION: Any differences between father and son shall upon request of either party be submitted for settlement to a committee of three disinterested persons who reside in the community and are familiar with the property. One member shall be chosen by father, one by son, and the third by the
other two members. A determination by a majority of the com-
mittee shall be binding on both the father and son. One-half the
cost of arbitration shall be paid by each party.

18. ADDITIONAL AGREEMENTS: 

In Witness Whereof, we have signed this lease this ............
day of ........................................, 19........

WITNESSES: