

Another option is to offer add-on or inclusive packages for multi-night guests. In this scenario guests pay more, but in addition to their room they receive a gift certificate to a local restaurant and two theater tickets. If you commit to helping your neighbors attract new business, chances are they will return the favor when recommending local lodging to their next patrons.

Another opportunity involves marketing in conjunction with special events and festivals in your community. The key to making package tours and cross promotion viable, of course, is making sure the legwork needed to arrange a package tour adds to your profitability. Another way to look at this is: if packages increase room nights, you are adding to your bottom line. It is far better to have guests stay longer with more opportunities to enjoy your area and cement their relationship with you, thus increasing the likelihood that they'll return.

To get ideas on the types of packages you might offer, visit the Classic Rosewood Inn website at www.thorwoodinn.com/packages.html

SETTING UP A FARMSTAY BUSINESS

As a working farm, you have the advantage of already running an established business.¹³ You can embed the farmstay enterprise into your existing farm business or create a completely separate business, perhaps even “doing business as” (DBA) a farmstay under another name.¹⁴ Regardless of your decision, you may wish to re-evaluate your business structure options, especially if you want to address liability risks that may be associated with your farmstay.

Business Structure Options

Businesses can be structured in many ways, each with advantages and disadvantages too numerous to address in this manual. These details and specifics are best left for CPA or business attorney professionals to address. Engaging one of these professionals when setting up your business is money well spent and can prevent you from facing unforeseen and costly headaches down the road. Be sure you find a CPA or attorney who understands farm and lodging businesses and who comes highly recommended. While all business structures require governmental record-keeping and forms to be filed, corporations and Limited Liability Companies (LLCs) involve additional legal and accounting requirements, but also provide liability protection to you personally.

The following page includes several common forms of business structures, broken down by the most recognized reason for choosing one over another: personal liability protection, a shield that prevents anyone with a court judgment against the business from touching anything other than the assets of the corporation. In other words, certain business structures better protect the personal assets of the officers, stockholders, and employees of the business, reducing the risk that your house, personal property, or bank accounts will be taken as a part of a settlement.

¹³ If you are setting up your farm and your farmstay at the same time, see *Building a Sustainable Business: A Guide to Developing a Business Plan for Farms and Rural Businesses*, published by the Minnesota Institute for Sustainable Agriculture, 2003—a 280-page, 5-chapter, step-by-step guide to developing a business plan with a focus on agricultural businesses. Includes worksheets and farmer profiles/testimonials. Available at Sustainable Agricultural Publications 802-656-0484.

¹⁴ In Minnesota, you can “do business as” a different name by filling out a Certificate of Assumed Name, paying a small fee to the state, and publishing notice of the name in an approved legal publication. For more information see: www.sos.state.mn.us/index.aspx?page=180.

Business Structures with No Personal Liability Protection

1. *Sole Proprietorship*

Many business owners who are self-employed set up their enterprise as a sole proprietorship, with few special requirements and no legal paperwork. This one person is responsible for the liabilities and debts of the business. If your business is sued, everything you own could be threatened by the lawsuit. Income from the business is reported as a part of the owner's personal income using the IRS Schedule C, and the sole proprietor pays self-employment taxes.

2. *General Partnership*

When two or more individuals own a for-profit business, typically operating under a written Partnership Agreement, the business is a general partnership. All partners are responsible for the liabilities and debts of the business. Income is reported on the IRS Schedule K-1 and may be subject to 15.3 percent self-employment tax. The partnership must file an annual return, Form 1065, with the federal government and possibly a state return.

Distinct Legal Entities Offering Personal Liability Protection to Shareholders

1. *C Corporation*

The most expensive and complex of business structures, a C Corporation is a legal entity set up within a given state and owned by shareholders of its issued stock. The corporation, not the shareholders or directors, is responsible for the debt and liabilities of the C Corporation. C Corporations must file articles of incorporation, hold director and shareholder meetings, file an annual corporation tax return, keep corporate minutes, and vote on corporate decisions. Income from C Corporations, after expenses have been deducted, is taxed both at the corporate level and at the individual level, on wages and dividends paid to shareholders.

2. *S Corporation, or Sub-chapter S Corporation*

Essentially a tax accounting classification, an S Corporation is a common stock-issuing, legal entity, income from which is taxed only once when it passes through to the employees or shareholders of the corporation on their personal income tax return. Like C Corporations, S Corporations must file articles of incorporation, hold director and shareholder meetings, file an annual corporation tax return, keep corporate minutes, and vote on corporate decisions. Most S Corporations can use the more straightforward cash method of accounting whereby income is taxed when received and expenses are deductible when paid. Unlike C Corporations, S Corporations are limited as to the number of shareholders they can have.

3. *Limited Liability Company*

The Limited Liability Company (LLC) is a separate legal entity established by filing articles of LLC formulation or a similar document in the state where it was formed. There are several ways, depending upon the number of LLC members, various classes of stock issued, and tax accounting method selected to properly meet tax liabilities, whether the LLC is treated as a partnership, C or S Corporation.

Despite the additional cost and regulatory paperwork for corporations and limited liability companies, many businesses choose one of these legal structures to control liability risk, sometimes in addition to purchasing business liability insurance. Some small enterprises, however, find that it's more cost effective to operate as a corporation or LLC than to take out costly business insurance policies, especially those that address livestock and other potential on-farm hazards. As an added precaution, these business owners may carry a separate \$1 million (or more) umbrella liability insurance policy should the unforeseen accident occur.

Employees

Depending on the situation and scale for your farmstay, you may decide to hire someone to help with your operations. Hiring employees to help manage your farmstay means that you will need to comply with federal and state labor laws. As an employer, you become responsible for paying half of your employees' Social Security and Medicare taxes as part of the Federal Insurance Contributions Act (FICA). You also need to pay state and Federal Unemployment Tax Act (FUTA) taxes in addition to workers' compensation fees, which vary by kind of work and wages. Some employers choose to provide or contribute to employee health insurance or retirement plans. All this can get complicated quickly, but there are accountants and payroll services that can help simplify the process.

It is important to understand that when you hire employees you are legally responsible for their safety while they are on the job. Additionally, while your employees are performing work related functions, your business is responsible for any accidents, injuries, or other losses for which they can be held liable. While there are some minor exemptions, generally all Minnesota business owners are required to carry workers compensation insurance for workers they hire. The state of Minnesota provides a helpful checklist for businesses hiring employees.¹⁵

Financial Considerations

While the excitement of starting a farmstay can be powerful, it is imperative to consider the financial aspects of the business. For most people, a farmstay must add net income to the farm. That said, the amount of income can vary greatly depending on many factors. Some farmers may be satisfied with adding a few hundred dollars a year to their net income while others may want to net ten or twenty thousand. It is important to be realistic and run your numbers using conservative estimates. A farmstay operation is not likely to be extremely lucrative, and it is probably best to start small and grow as you gain experience and customers. On the next few pages are some sample financial documents to help get you thinking about what you need to consider.

Financing the Farmstay

How much money you need to start your business depends on the type of farmstay you are starting, how well you save money prior to launching it, how creative you are when incurring start-up expenses, and/or your ability to tap funds from financial institutions, family members, or friends. Few successful ventures start big, and all businesses change over time. An advantage to starting small is that you and your market can readily adapt as you, your farm, and your market change.

¹⁵ http://www.positivelyminnesota.com/Business/Starting_a_Business/Basics_for_Employers/Checklist_for_Hiring_an_Employee.aspx.

Some farmstays have been able to start up with less than \$1,000, paying mostly for registration fees, a simple website, and perhaps an investment in a couple of new beds for guests. Many farmstay owners invest an immense amount of sweat equity—personal labor without pay—when launching their business. Instead of hiring painters for remodeling or contracting for Internet design services, these owners do it themselves.

Depending on the scale and scope of your operations, there are several financing options when funds are needed. The vast majority of small businesses start by drawing financial resources from owners' savings or assets. In essence, the business owner acts as a bank by personally making a loan to the business. For example, an owner might loan the farmstay business \$10,000 at 4 percent interest to purchase beds and make lease-hold improvements to several rooms (perhaps adding private bathrooms) used for business purposes. Every year, the business pays interest to the individual personally on that loan until it's paid off.

If you have a well-developed business plan, local financial institutions like banks, credit unions, or community-based revolving loan funds may be a source of financing. For these institutions, your collateral and credit history, as well as their experience with financing lodging operations, will influence their decision of whether or not to loan you money.

Family members and friends may provide a simpler form of financing, but approaching them can strain relationships, and you need to evaluate what would happen if the business falls behind on the loan payments. If you do have family and friends who share your enthusiasm and are sold on the success of the business, it is important to negotiate the terms of the loan and get agreements in writing.

Profit and Loss Statement

A business is summarized by an income statement reflecting revenues and expenses, also called a Profit and Loss Statement (P&L), as well as by a balance sheet (BS) reflecting the assets and liabilities (and equity) of the business. The difference between assets and liabilities is the net worth of the business. Most small businesses are set up to have a calendar year ending December 31, rather than a fiscal year that is a period of 12 months starting at some date during a current year.

On the next page is a sample Profit and Loss statement (income statement) for a two-guest room farmstay bed and breakfast that also has a small gift shop and sells fruits and vegetables to guests. It is provided to illustrate revenues from the farmstay offset by expenses associated with running the business. Many small businesses will choose to reinvest revenues back into the business, so profits may be small while the business develops. For more information related to these calculations, see the book, *ECOpreneur*, listed in the Resources Section of this Manual.

Sample Profit and Loss Statement (Income Statement)

Revenues

Farmstay lodging (200 nights at avg 108/night)	21,676
Gift store purchases	1,161
Fruit and vegetable purchases	593

Total Revenues **23,430**

Expenses

Compensation of owners	4,000
Repairs and maintenance	1,834
Rents	3,600
Taxes and licenses	1,714
Interest (on loan to owners)	320
Depreciation	1,712
Advertising	946
Other itemized deductions	
Government filing fees	311
Legal and accounting	550
Telephone/Internet	1,619
Memberships	441
Food for farmstay	747
Credit card fees	760
Supplies	894
Office expenses	322
Utilities	514
Insurance	471

Total Expenses **20,755**

Net Revenues (profit) **2,675**

Sample Cash Flow for a Farmstay Bed & Breakfast that has a mini retail store and offers fruits and veggies for sale.

Business Components	Jan	Feb	Mar	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec	TOTAL	%
Bed & Breakfast	150	963	845	1285	3587	4119	3873	3291	1522	1591	300	150	21676	93%
On Farm Retail					176	324	289	252	120				1161	5%
Direct Sales					15	45	198	225	100	10			593	3%
Cash Receipts	150	963	845	1285	3778	4488	4360	3768	1742	1601	300	150	23430	
Cash Disbursements	2045	298	934	645	1975	3380	3790	2990	3201	269	355	873	20755	
Net Cash Flow	-1895	665	-89	640	1803	1108	570	778	-1459	1332	-55	-723	2675	

Cash Flow

While income and balance sheets are important to your understanding of how your business functions and are required for federal and state tax filing if your business is formed as a corporation or LLC, cash flow is one of the more challenging aspects of getting a new business going. Too often, not enough cash is kept in reserve or there's limited access to additional capital, forcing the business to close before it is effectively marketed and a customer base established.

The start-up phase for many businesses is three to four years, so financing and cash flow considerations are paramount during this period. The robustness of your existing farm business may help maintain sufficient cash flow until the farmstay has developed an adequate market to support itself and generate consistent profits.

To the right is a sample cash flow statement for a two-guest room farmstay bed and breakfast, provided to illustrate revenues may be highly variable from one month to the next. Therefore, it's essential that cash reserves are available to cover expenses that may come up in months where revenues are nominal. For more information related to these calculations, see the book, *ECOpreneur*, listed in the Resources Section of this manual.

Insurance and Liability

Liability issues are complicated and can be arduous. Thinking about possible misfortunes that might occur is a great way to dissolve the enthusiasm that drives aspiring farmstay hosts. Prior planning, though, is one way to safeguard your new venture from potential disaster. Should an accident happen, having appropriate liability coverage may make the difference between the future success and failure of your enterprise.

Liability is a complex legal concept and the information in this manual is in no way meant to substitute for professional legal advice. The number one rule regarding liability coverage is: Do not make assumptions about what your insurance policy covers. Ask your insurer specifically if the activities happening on your property are covered by your policy. If one insurance agency does not or will not cover the activities you are engaged in, shop around for an agency that is familiar with small farm businesses or bed and breakfast operations and can offer the protection you need. Industry association like the Minnesota Bed and Breakfast Association, the Congress of Minnesota Resorts, and the Minnesota Resort and Cabin Association may be able to point you to helpful insurance agents.

Types of Liability

Most farms carry some sort of farm insurance, but when you add new enterprises to your farm you need to talk with your current insurance agent to see if and how these new enterprises will affect your policy. The main liability issues involved with adding a farmstay enterprise will likely come from having more people on your farm—this is called premises liability. You also might need to consider product liability if you will be selling food or products from your farm. How you structure your business may also help mitigate liability issues as addressed in the business structure portion of this manual.

Premises Liability

In the transition to an agritourism enterprise of any sort, including a farmstay, you will become responsible for the safety of more visitors to your property. The threat of liability can be reduced if you identify and eliminate potential safety hazards.

Carefully evaluate what areas of the farm visitors will be allowed to access and how you will restrict visitor access to potential hazards. Ask yourself if you are willing to accept the liability of allowing visitors to interact with large animals. Will visitors be allowed near any potentially hazardous farm machinery? If performing farm labor will be part of your visitors' experience, how might this expose your visitors to risk? Are there any natural hazards on parts of the farm where visitors could potentially be hurt? Can any of these hazards be reduced or eliminated by reasonable measures?

Once you have answered these questions and decided what action you are willing to take to minimize safety threats, be open with your insurer about what threats still exist and what action you have taken to eliminate them. Honesty with your agent is crucial to getting coverage for the safety concerns that exist on your farm. Your insurer knows as well as you that safety threats can never be eliminated completely; this is why they are in the business of protecting their clients from the risks associated with premises liability.

All of these scenarios represent a trade-off between how much risk you are willing to accept (which will be reflected in insurance premiums) and the type of visitor experience you are trying to create on your farm. Perhaps the opportunity to ride horses, milk cows, split wood, fish in rocky creeks, or hunt for wild game will not be activities you choose to feature on your farm because of the risks and liability they present. Or, perhaps, they are key features of the business you want to create, and you are ready to accept a higher insurance premium. You may also choose alternative activities that are less risky, like picking strawberries or apples, or if you attract families with kids, allowing children to play on a pile of straw bales. Be clear with your insurance agent about the activities your visitors will engage in to ensure that your policy covers the liability associated with those activities. If your current insurer doesn't offer a competitive rate, shop around — rates vary dramatically from one insurer to the next.

Insurance Riders

On any private farm, especially those with the attractive qualities of a farmstay, there may be certain events or circumstances for which you would want to purchase additional coverage beyond your normal policy. Such events may include gatherings you host on the property, such as farm festivals, weddings, or company retreats. Hosting such events can be a great opportunity to make additional income from your land, but can also present additional liability concerns. If you want to host a gathering like this, talk with your insurer about adding an insurance rider to your policy for such events that are not part of your everyday business enterprise. Depending on the activity, you may also need to gain approval from your County Zoning Board.

If your insurer has no such product available, shop around for an insurer that does. Generally, for one-time events like these, you can add extensive liability coverage for a rather low cost. If the price of an insurance rider ultimately is too costly, it may be a cost you can pass on to your customer—such as the couple hosting a wedding or the company hosting an annual picnic. You may even require that your customer hosting the gathering purchase the rider from his or her own insurer. In this last case, a policy can be written where any injured guests will have to seek damages from their host's insurer first before collecting anything from your personal insurance policy. This sort of agreement will provide you with an added layer of protection and encourages your guests to act responsibly.

Loss of Rent Insurance

If you have made a considerable investment in your farmstay, you may want to consider Loss of Rent insurance. This type of insurance covers property owners from loss of rent if their farmstay is damaged (e.g., by a storm, fire, or fallen tree).

Product Liability

If you are a farm selling directly to customers, you have probably addressed product liability. Product liability is the responsibility a producer has to provide a product that is safe. In the case of food, that means a product that is free of pathogens and will not cause food-borne illnesses. Many farmers' markets, food distributors, and grocery stores require product liability insurance coverage for all their vendors. If you are selling product directly from the farm, some homeowners or property insurance packages may include product liability coverage—but make sure this is spelled out in your policy.