Getting on Solid Ground

An Overview of 15 Ways to Secure Land

Excerpted from the ***Farmer's Guide to Securing Land***

Produced with Support of USDA, Western SARE

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"Cultivators of the earth are the most valuable citizens. They are the most vigorous, the most independent, the most virtuous, and they are tied to their country and wedded to its liberty and interests by the most lasting bands."
–Thomas Jefferson

Secure access to affordable farmland is one of the most significant challenges facing today's new farmers (and there are many). The success and sustainability of an agricultural endeavor often depends on land security, as does a farmer or rancher's willingness to be a good land steward. Most farmers and ranchers would prefer to own the land they work; but in the face of high land prices and economic uncertainty, ownership may not always be practical or even wise. The purpose of this overview of land tenure models is to widen the scope of options farmers and ranchers can consider in their quests to creatively and affordably secure agricultural land.

More in-depth information about each of these models can be found in *The Farmer's Guide to Securing Land,* a 183-page handbook for farmers and ranchers published by California FarmLink in 2008. The handbook includes general information about agricultural land tenure in California; descriptions of ways to lease, own, and otherwise creatively secure farmland; case studies illustrating those approaches; and sample language from actual documents concretizing these land tenure transactions. To order a copy of the Guide, call California FarmLink's main office at (707) 829-1691 or email info@californiafarmlink.org.

Land Tenure, Defined

The term "tenure" comes from the Latin word *tenēre*, meaning "to hold." Land tenure is the act of holding, or the right to hold, land—whether in "fee simple" ownership or via some other agreement with the owner of that land. Old English Common Law introduced the concept of land ownership to the United States, in which land can be bought and sold as private property. The following fourteen legal models for land tenure, from "fee simple" ownership to easement-encumbered ownership, and from long-term to short-term leases, are all operable within this now American philosophy and legal structure of land ownership.

How *Not* to Use This Material—A Disclaimer

Far too often, we hear of farmers or ranchers with only verbal agreements securing their access to a piece of land. At California FarmLink we discourage this because human memory is a funny thing—differing recollections of a so-called "agreement" may easily lead to conflicts, which can lead to failed businesses, broken friendships, lawsuits, and much grief. So remember—when negotiating tenure on a piece of farmland, even with a good friend or relative, a written and signed document is *essential.*

A qualified professional (often a realtor or attorney) should review your documents before you sign them. With some models, such as the cash lease, you will have no trouble finding a qualified professional to review your work. At California FarmLink, we provide technical assistance on land tenure. We will be happy to assist you with your particular opportunity and/or direct you to qualified professionals as needed. We have done our best to provide you with accurate information, however we must state for our legal protection as well as yours that we cannot be responsible for documents, agreements and transactions you enter into based on the information provided in this overview. All final documents should be signed only after being reviewed by a qualified professional.

1. Cash Lease Model

A long-term lease of 5 to 30 years may be the optimal tenure agreement for many farmers with limited financial assets. It is crucial to protect oneself to the degree possible from changes in ownership impacting the lease. In signing a cash lease, the beginning farmer is calculating an ability to cover a fixed payment for the term of the lease. The funds are due to the landlord regardless of a good year, a bad year or a longer time to get the operation going than planned. While lease agreements can vary in terms of complexity, at a minimum they should address responsibilities for maintenance, repairs and dispute resolution. Cash-rent leases can be negotiated based on agreed understanding of local market value. Establishing a fair rate can be challenging. The California Association of Farm Ranch Managers and Appraisers provides an annual review of lease values by crop and land type for most California counties. This information is available through California FarmLink, please visit our website at www.californiafarmlink.org. Rates will depend not only on the quality of soil and availability of water but also on outbuildings, irrigation systems and other infrastructure.

Today farmers establishing their own operations are often 30-40 years old or more. A 30 year lease is appropriate to meet their goals of farming until retirement age. Long-term leases of up to 99 years are legal in some states. We are not familiar with leases longer than 51 years in California.

2. Crop-share Lease

A crop-share agreement or share-rent is a means for compensating a landowner for use of the land while sharing the risk. Payment may include a share or percentage of crop, for example 20% of the walnuts harvested, or a percentage of the gross or net income. A crop share requires a level of trust between lessee and lessor which may include sharing financial or tax records. By agreeing to pay the landlord based on how much crop comes in, the beginning farmer will owe more if there is a great harvest and less if there is a poor year. Determining a percentage fair to both parties can be done based on knowledge of the "going rate" or through worksheets spelling out the specific contributions of each party. Paying rent by committing a share of the crop may help entice landowners to lease when they don't consider the going rate for cash rental to be significant. For example, if cash rent is valued at $500 per acre per year, a landlord may prefer to share risk assuming as much as $2-3,000 if crop share rent were calculated at 10% of gross sales on a produce operation. A crop-share lease looks almost identical to a cash lease except in the payment section where the share is described rather than a fixed number.

3. Cash Lease from Governmental and Non-Profit Entities

Many governmental and non-profit entities have significant farmable acreage that they can lease to private individuals. The availability of infrastructure including wells, barns and fencing varies from place to place. These leases are often publicized only briefly or through their own established networks in the agricultural community. A proactive, beginning farmer should make an effort to call or write the California FarmLink office to inquire with appropriate program staff. While a significant waiting period may be required, once a lease is obtained, an agreement running 2-5 years with the opportunity to renew may be possible. California FarmLink is developing a list of government and non-profit entities that lease to beginning farmers.

4. Ground Lease

Ground leases are a well-established form of land conveyance and ownership. A ground lease normally has a term, which is at least ten years longer than a long-term mortgage. This makes the usual term from 40 to 99 years. Because of the length of the lease, it is prudent to put a lot of detail into the drafting of the lease. An accurate legal description is essential. In California, it is also prudent to obtain a title report from an established title company, and to obtain a policy of title insurance that guarantees title is as shown in the title report. The lease should be recorded. If the actual lease is deemed too cumbersome to record, a memorandum of lease that recites the parties, the term and the correct legal description can be used to notify people about the lease.

A ground lease can be a basis for getting a mortgage loan to build a house.

5. First Right of Refusal and Option to Purchase

A clause in the lease giving the lessee the first option to buy if the property goes on the market is important for protecting a young farmer's investments in the land. First option to purchase can be included as a part of any lease agreement whether payment terms are cash or crop-share. Having an option means little if the beginning farmer is not positioned to be able to exercise the option and get financing for purchase in time to exercise the option.

6. Fee-title Purchase

This is the standard means of purchasing a farm: find the money, make the offer and purchase the farm. This is increasingly difficult as land prices increase and agricultural lenders want to see a demonstrated track record of successful farm business management. Such lenders require a credible cash-flow projection to determine whether to provide financing. The lender will analyze the applicant's ability to make money from the specific piece of land to be purchased. One variation suitable for purchases of relatively small acreage (i.e. 2-15 acres) is to seek financing assistance from a mortgage broker or bank for a single family residence. By demonstrating significant income from off-farm sources based on a track record of maintaining an off-farm job, the purchaser may qualify for a home loan. This may allow the purchaser to obtain a lower interest rate. This also circumvents the hurdle of demonstrating significant farm management experience.

We recommend negotiating fees with either a realtor or lawyer in order to put together a purchase agreement that will pass legal muster.

7. Fee Title Purchase with Sweat Equity

Equity in general can be thought of as the portion of an asset's value that is owned by the proprietor or shareholders. Equity can be purchased outright or gained passively as a result of external market forces, gift or inheritance. With sweat equity, equity is earned by "sweat" or hard work. This can be structured in several ways.

Sweat equity for a farmer can be defined as ownership in an asset gifted to or negotiated with a farmer to provide that farmer with an ownership stake in the land or farm operation.

Acquiring ownership of land can be accomplished over time with a flexible seller that recognizes the contribution the buyers have made or will make through their labor. With a "sweat equity" purchase, the buyer is paying off all or a portion of the agreed upon cost of a property through labor. Parents may make a "sweat equity" agreement with a son or daughter stating that, in addition to wages for working on the farm, we will give you 5% ownership the for every year you work. Through such an arrangement, the son or daughter could become a full-owner over 20 years or could inherit at the parents' death or could buy the parents' remaining interest when it was smaller. Alternatively a sweat equity deal can be negotiated as part of a purchase involving a cash down payment.

8. Land Contract Sale

An installment sale or land contract sale is an agreement through which the seller (original owner) of the land agrees to finance the sale to a new buyer. The new buyer moves on to the land and begins making payments based on an agreed upon interest rate and terms.

This approach can benefit a beginning farmer who would not have to approach a commercial or governmental lender for a traditional loan. The seller, in turn, benefits by limiting capital gains and income tax liability. In addition, if the seller finances the sale, or "carries the note," through an installment sale and the beginning farmer defaults, the land goes back to the seller who can then select a new buyer. The danger for the buyer is that a default near the end of the contract leaves the buyer with nothing, unlike a default near the end of the term of a deed of trust.

9. Agriculture Conservation Easement Sale

The dream of owning the land remains powerful for many beginning farmers regardless of the rapidly increasing prices and advice from USDA and commercial agricultural lenders that leasing or other tenure models are often a much more sound business decision. With an Agricultural Conservation Easement (ACE), a third party group maintains the development rights while the farmer owns the farming and water rights and all other private property rights including exclusive use. For beginning farmers who seek to own land, obtaining land with a conservation easement that restricts their ability, in perpetuity, to pursue residential or commercial development on the property can help make a purchase affordable. The California Department of Conservation, USDA Farmland Protection Program and various local government and private sector groups are supporting the purchase of conservation easements on agricultural land.

10. Easement Sale as Part of Farm Succession Plan

Conservation easements in California have typically been utilized to help existing landowners protect land from development while managing tax liability or minimizing debt. An important variation on this theme is to purposefully treat the sale of a conservation easement as a tool to achieve goals of transferring the farm from one generation to another. Sale of an easement can be used to buy out a non-farming heir, purchase land or other assets to provide on-farm heirs resources to grow the farm business; or cover the retiring generation's retirement needs so that they are no longer dependent on farm income to cover essential living expenses. In these ways the funds received from sale of an easement become the missing piece in a plan to transfer farm assets in such a way that facilitates ownership for the next generation.

11. Transfer of Farming Rights

A transfer of farming rights is an innovative approach that promises to address the interrelated challenges of securing long-term land tenure for agriculture; helping farmers build equity they can realize for retirement; and achieving affordable asset ownership in locations where market land values have skyrocketed far beyond the capacity of a farm business to justify land purchase. The transfer of farming rights is a deed restriction that a farmer can purchase from a landowner in order to secure the right to farm in perpetuity. A similar model has been used de facto in the timber and mining industries. The right to farm is transferred to a private individual through an easement recorded with the county as a deed restriction. The right to farm stays with the farmer owning it, regardless of whether the ownership of the other rights in the "bundle of rights" associated with real property changes hands one or more times.

12. Farmer Secures Tenure Through Partnership with a Residential Development

Farmland prices have soared out of reach of most farmers, due at least in part to increased demand for housing. Housing developments continue to spring up, despite heavy environmental and even social costs, causing direct threat to farmland. In efforts to meet housing demand while maintaining farmland and urban growth boundaries, creative developments have begun to emerge—integrating higher-density housing with productive, agricultural landscapes. This represents a unique opportunity for a beginning farmer seeking to secure affordable land tenure.

We are aware of several cases in which a private developer or co-housing organization manages to incorporate active farmland into a new housing development. These developments, found both rurally and in cities, can generate great appeal for potential homebuyers wishing to live near working farms. When appropriate farming practices are prescribed, incorporated farmland can help create harmonious urban growth boundaries, increase public awareness of agriculture and food systems, and actually cost less than more standard development models—often reinforcing county and municipal general goals.

There are benefits to farmers of the next generation as well: When strong tenure and equity-building options are reserved for them, small- and medium-scale farmers can actually afford to reside in lively communities, near markets for their products, and have ownership in a home and/or improvements on their farmland, without necessarily having to purchase the land itself.

How is accompanying farmland allocated and managed in these innovative developments? It may be owned by the developer and leased out for farming by a property management company owned jointly by the homeowners and managed by a homeowner's association owned privately (by a resident farmer, for example) but maintained available for agriculture by easement donated to a city, other public agency or nonprofit as part of the approval process, and managed by paid staff or through a long-term lease agreement.

13. Teamwork for Tenure: Shared Ownership Models

In forming a partnership, corporation or limited liability company (LLC), chief considerations include how will various investors share: ownership, control/decision-making, and risk or liability. For example one group may choose to have "silent partners" who invest cash but do not have a say in day-to-day operations of the farm. Some partners may have more off-farm assets than others and therefore might be taking on an unequal level of risk if the farm were sued. By answering these questions, one can determine the best legal entity to do the job. The LLC has become popular over the last several years as a means of meeting many goals of shared ownership while limiting bureaucratic requirements and cost. One option is for an LLC to own land and lease it back to a farm entity. This may offer several advantages.

First, multiple investors can share ownership in the form of shares or stock in the land asset. With an LLC one owner can choose to sell his or her shares at any time and other members can either buy the departing shareholder out or find another investor to purchase those shares. This allows the land to continue to benefit LLC shareholders regardless of changes in the personal goals or financial situation of one individual. By leasing land to the farming entity, the shareholders are assured the opportunity to gain equity and obtain income tax advantages from deducting mortgage interest (a portion of which can be considered an expense against the lease income). In addition, this type of entity can be used to separate decision-making among active farm managers who need to be involved in day-to-day production and marketing decisions and absentee land-owning shareholders. Absentee shareholders might include a parent, CSA member or "angel" investor. Much of what is described here as benefits of an LLC can be found in other forms of incorporation or partnership agreements.

14. Silent Partnership to Buy Land

Many beginning farmers committed to land ownership are unable to secure down payments or viably manage mortgage payments, but individual, non-farming investors can sometimes offer the "leg up" necessary to make a land purchase. In turn, they may benefit over the long term due to a share in that farmer's business, tax benefits resulting from being part of farm-business partnership, real estate development on a portion of the land, or simply the intangible reward of knowing that they have played a role in the development of a more sustainable agriculture. If the land and business holding entities are set up so that decision-making control stays with the farmer and the investor does not have a formal voice in the ongoing management, the investor is referred to as a "silent partner." In return for an ownership stake in the farm business, the investor is motivated to offer land buy-back terms favorable to the farmer, thus maximizing the opportunity for the farmer to succeed.

15. Community Land Trust

A community land trust (CLT) is a non-profit organization that owns real estate to benefit the local community by enabling long-term low cost ownership. The organizations are democratically controlled and serve to provide long-term housing and farmland tenure. A CLT encourages good land stewardship and makes land more affordable because the common land is held by a trust as land designated for the broader community's use while individual families or farmers hold long-term leases on a plot of land. Because CLTs are able to provide long-term leases they have the ability to preserve affordability over a long period of time. Land, a limited natural resource is removed from the market and held in trust by a democratically structured non-profit. The value created from the labor applied to the land (agriculture crops and buildings) is private equity and becomes a liquid asset to the persons who are investing time and resource into the infrastructure value and is exchangeable in the market place with limited equity potential. Generally a CLT is organized as a tax-exempt 501(c)(3) non-profit organization. In some cases a 501(c)(2) is established as a title holding company to administer property leaseholds that would jeopardize the tax-exempt status of the 501(c)(3).