

# AGRICULTURAL ALTERNATIVES

## Owning and Leasing Agricultural Real Estate

Land is the basic resource that distinguishes agriculture from most other types of businesses because it is required for the production of crops and livestock. Land is the most valuable asset on the balance sheet of most farmers.

How much land you need and how you acquire it are two of the most important decisions for a farm operator. Not having enough land can limit the efficiency of the other resources you use on the farm and may severely limit your ability to expand your business in the future. Having too much land may limit your ability to manage it effectively and may cause cash flow problems that limit your ability to make other investments.

Acquisition of land should be thought of in terms of control; control can be in the form of ownership or leasing. Most farmers find that a combination of both ownership and leasing is desirable, especially when capital is limited. For many new farmers, especially in areas where land is quite expensive, leasing land is often the best option. Some farmers choose to own only their home and a limited amount of land for



barns, crop storage, machinery sheds, livestock facilities, and other real estate improvements. They then lease the bulk of their land for crop production, allowing them flexibility to adjust their farm size as conditions warrant.

Owning land has the following advantages:

- It eliminates the uncertainty of losing a lease and the impact that would have on the overall operation.

*This publication was developed in cooperation with University of Maryland Cooperative Extension and is intended to provide general information about legal issues regarding agricultural land leasing and real estate purchases. It should not be construed as legal advice or cited or relied upon as legal authority. State laws vary, and no attempt is made to discuss laws of states other than Pennsylvania. For advice about how the issues discussed may apply to your individual situation, please consult an attorney.*

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- Accumulated equity in land provides an excellent source of collateral for borrowing money.
- Decisions about management of the land including enterprise selection, conservation practices, and use of soil amendments are solely the choice of the owner.
- Land provides a hedge against inflation over the long run.
- It ensures that the operator will receive the benefit of the labor and investment made in improvements.

Owning land also has some drawbacks:

- The principal and interest payments associated with purchasing land can create cash flow problems and limit the ability to make other purchases. Restricting the amount of working capital can severely affect the potential profitability of a beginning farmer with limited capital.
- Land has a lower return compared to many other uses of capital like machinery, livestock, and annual operating inputs,
- Attempting to own all land used on the farm may restrict the farm to a size that is inefficient and unable to employ new technologies effectively.

Leasing land has the following advantages:

- When capital is not tied up in land purchases, it can be used to purchase other important assets including machinery, livestock, and annual operating inputs.
- Many new and beginning farmers may lack management skills that may be provided by a knowledgeable landlord (who in many cases previously farmed the land).
- Because most leases are short-term (often only one year), changes in business size or location can be made fairly easily by giving up old leases or leasing other land.
- Leases are a more flexible financial obligation than mortgages and can be renegotiated each time the lease is renewed.

Leasing land also has drawbacks:

- Because most leases are short term, there is uncertainty about whether all or a portion of leased land

could be lost on fairly short notice and how this might affect the future of the business.

- Landlords are often reluctant to make improvements to land or buildings on leased property. Tenants usually cannot justify making improvements because of the uncertainty regarding future control.
- If land is not owned, equity can only be accumulated in machinery, livestock, or savings. This can limit the ability of farmers to borrow money to reinvest in their business.

There is no clear advantage to owning versus leasing agricultural real estate. Control is probably the most important consideration and depends greatly on the individual operation. Having a balanced combination of owned and leased land is important to effectively use available labor, machinery, and capital without generating excess financial risk for your business.

## Leasing of Agricultural Real Estate

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According to the 2012 Census of Agriculture, leased farmland accounts for 31 percent of all farmland in Pennsylvania. Leases for agricultural real estate can provide an easy mode of entry for beginning producers or established farmers wishing to expand their production. Many lenders may require new producers to lease farmland in order to develop and demonstrate the skills necessary to take the big step of purchasing their own farm. For many producers, the goal may be to eventually own farmland. This publication provides an overview of various land leasing issues facing agricultural landowners and agricultural land tenants, raises issues important from both a landowner's and tenant farmer's perspective, and gives a brief overview of issues involved in purchasing land. The economics of whether to purchase land or to lease it will not be discussed; you should work closely with your lender to determine if purchasing farmland is the right step for your farming operation.

## What Is a Lease?

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A lease is a legally enforceable contract allowing the owner of real property, equipment, and/or livestock to convey the right to use that property to a person in exchange for rent. The lease defines the rights between the landlord and the tenant, and defines how the landlord/tenant relationship will operate.

A lease needs four essential elements to be considered valid: (1) a contract; (2) a payment provision or “how much rent is owed”; (3) the transfer of rights to use and possession, and control of the property to the tenant; and (4) intent to transfer rights to use, possession, and control of property back to the landlord when the lease terminates. A lease demonstrating these four elements will be considered valid. Note that “written” is not a necessary element; while this issue will be further explored, a written lease does provide a record of the terms agreed to in the lease.

## Types of Leases

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Landlords and tenants have a variety of lease types from which to choose, depending on their goals. Three common arrangements between landlords and tenants are the *cash lease*, the *flex lease*, and the *crop-share lease*. Parties will want to pick the best arrangement that suits their needs.

Under a *cash lease* or a *fixed cash lease*, the tenant pays the landlord either a cash sum per acre or lump sum for the rights to use the land and other farm resources. Landowners under this type of lease need not concern themselves over the types of crops grown or amount of

production costs, nor about price and yield fluctuations. For a tenant, a cash lease allows the tenant to make all the management decisions, provides an incentive for the tenant to reap the highest yields possible, and allows the tenant to retain windfall profits from yield or price increases.<sup>1</sup> Worksheets available through organizations such as **AgLease101.org** can aid both parties in calculating a fair rental rate.<sup>2</sup> Cash leases are by far the most common type of lease used by farmers in Pennsylvania.

A hybrid cash rent lease is a *flexible cash rent lease* or a *flex lease*. A flex lease is similar to a cash lease in that the landlord charges the tenant an amount per acre. Unlike a cash rent lease, rent under a flex rent lease can fluctuate up or down depending on crop yield, market price, or a combination of both.<sup>3</sup> A flex lease allows the landlord to gain when market prices or crop yields increase during the crop year. But in return for the possible increase in rental payments, a landlord also loses when market prices or crop yields decrease. Under a flex lease, the tenant also benefits from the possibility of lower rent payments during low yield or low price years. The tenant is required to share gains, however, during high yield or high prices years through higher rental payments. Again, worksheets are available through **AgLease101.org** to aid in calculating a fair flex-cash rental rate. These types of leases have increased in usage in recent years because of high commodity prices and higher yields for many agronomic crops.

Under a *crop share lease*, a tenant pays the landowner a certain percentage of harvested crops. In return, a landlord allows the tenant to use the land and may pay a percentage of certain input costs. The percentage of both crops and selected expenses are usually based

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<sup>1</sup>For a more detailed review of the advantages and disadvantages of a cash lease for either party, see North Central Farm Management Extension Committee, *Fixed and Flexible Cash Rental Agreements For Your Farm* (December 2011), available at **aglease101.org/DocLib/docs/NCFMEC-01.pdf**.

<sup>2</sup>See North Central Farm Management Extension Committee, *Fixed and Flexible Cash Rental Agreements For Your Farm* (December 2011), available at **aglease101.org/DocLib/docs/NCFMEC-01.pdf**.

<sup>3</sup>For information on how to set a flexible rental rate, see North Central Farm Management Extension Committee, *Fixed and Flexible Cash Rental Agreements For Your Farm* (December 2011), available at **aglease101.org/DocLib/docs/NCFMEC-01.pdf**.



on local custom. For example, tenant agrees to crop share rent landlord's farm for corn production. Terms of such a lease might require tenant to give landlord 25 percent of the corn crop produced on landlord's farm, in exchange for use of the farm and landlord paying 25 percent of the drying and herbicide costs. Crop share leases are common in the midwestern and southern United States, but are not used very much in Pennsylvania.

## **Written versus Oral Leases**

Written leases are mandatory in certain cases under Pennsylvania's Statute of Frauds. This law requires leases of more than 3 years' duration to be in writing and signed to be valid, while leases less than 3 years'

duration may still be oral. For example, suppose a landowner orally agrees to rent his farm to a tenant for 3 years, with an understanding that the lease can be renewed after year 3. The lease will be valid because the lease can be performed within 3 years. Even though the lease can be renewed at the end of the 3-year period, it does not mean it *will* be renewed. But if the landowner orally agreed to rent his farm to the tenant for 6 years, this lease *must* be in writing and signed to be valid and enforceable in Pennsylvania.

Some exceptions to the Statute of Frauds may render an otherwise invalid oral lease enforceable. Pennsylvania courts have allowed the Statute of Frauds' writing requirement to be waived in some cases. A Pennsylvania court has ruled that an otherwise invalid oral agreement be upheld in some cases where a tenant

has made rent payments and the landlord accepts those rents, recognizing the existence of a lease (*Blumer v. Dorfman*, 1972). For example, suppose a tenant and landowner have an oral lease to rent a farm for 5 years. The tenant takes over the farm, pays rent on time, and the landowner accepts the rent. As such, the landowner would not be able to argue the oral lease is invalid under the Statute of Frauds. A written agreement, however, provides both landlord and tenant greater legal certainty especially when the lease term exceeds 3 years, because parties do not want to rely on a court to find their lease an exception to the Statute of Frauds.

## Lease Termination

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Parties can specify how the lease will be terminated in the lease. This is especially important if the tenant needs more time to vacate the premises than state law allows. If the lease specifies how it is to be terminated, the exact procedure must be followed; courts are traditionally not forgiving of parties that do not follow the proper notice termination procedures. For example, if the lease states that notice should be given “in writing and delivered by certified mail within 6 months before the lease terminates,” then notice must be given within 6 months of the end of the lease by certified mail. A *sample termination letter* that can assist landlords or tenants in terminating the leasing arrangement can be found in the back of this publication.

When a lease contains no termination process, the parties must follow state law. In cases where a lease is about to expire and (1) the landlord does not wish to renew, (2) tenant has breached the lease, or (3) tenant has failed to pay rent to terminate the lease, landlords will need to give the proper notice (P. S. Ann. § 250.501(a)). When the landlord wishes to terminate the lease for any of these three reasons, then the landlord must give at least 15 days’ notice in writing to terminate the lease for all leases of less than 1 year duration (P. S. Ann. § 250.501(b)). For all leases longer than 1 year, the landlord must give 30 days’ notice in writing to terminate the lease. State law has no similar provisions for tenants (P. S. Ann. § 250.501(b)).

Because state law only requires 15 to 30 days’ notice to terminate leases, agricultural tenants who may require more than 30 days to vacate the leased property should consider including a termination process in the lease. Section 250.501(e) does allow for a tenant to waive the statutory time in a lease agreement. Tenants would want to consider their operations and equipment needs to determine if the termination process needs to be longer to accommodate their agricultural operation.

## Growing Crops

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What happens if the lease terminates and tenant has not had the opportunity to harvest crops on the leased property? This question can be answered in multiple ways depending on the type of crops being grown, language in the lease, and other factors. The best way to resolve this issue is simply to include in the lease language that allows a tenant a reasonable time to harvest growing crops after the lease terminates, or similar language allowing the tenant time to come back on the leased property to harvest growing crops after the lease has terminated.

If the lease is silent as to a tenant’s rights to growing crops after lease termination, then the tenant’s rights to the growing crops would depend on how the lease terminates. When a lease is for a term of years and the tenant knows the date the lease will expire, a tenant will *not* be able to harvest crops maturing after the lease expires (Am. Jur.2d Crops § 27, 2014). For example, suppose a tenant’s lease will terminate on December 31, and they plant a wheat crop to be harvested in June, 6 months after the lease has terminated. Because the tenant knew the date the lease terminated, traditional rules will not allow them to harvest the wheat crop.

When the lease is for an uncertain term (both landlord and tenant are not sure of the end date), the tenant traditionally has the right to harvest the growing crop, absent an agreement to the contrary (*Commonwealth v. Peterman*, 1938). This rule applies to “away-growing crop,” or a crop growing at the ter-

mination of the lease. Pennsylvania has traditionally viewed annuals, plants that complete their life cycle in 1 year and are produced by the labor of the tenant, such as wheat, corn, and vegetables, as “away-growing” crops to which the rule can apply (*Swanson v. Carlson*, 1987). Pennsylvania courts have rejected applying this rule to hay crops (*Reiff v. Reiff*, 1870).

## Improvement/Fixtures

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A *fixture* is personal property attached to the land that is regarded as a non-moveable part of the real property. Examples of a fixture would include buildings, cattle lots, or below-ground level diesel and oil storage tanks. In Pennsylvania, unless the lease specifies otherwise, tenants have the right to remove those tenant’s fixtures that are necessary to the operation of his/her business at the end of the lease (*Cattie v. Joseph P. Cattie*, 1961). Of course, a tenant does not have the right to remove fixtures that the landlord has placed on the property. Before adding fixtures to the leased property, tenants should consider drafting an agreement making clear which fixtures belong to the tenant, that the tenant will remove the fixtures at the end of the lease, and the condition the property will be returned to when a fixture is removed. Drafting this agreement early will reduce potential problems down the road.

## Good Husbandry Practices

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Pennsylvania courts view agricultural leases to include the implied duties that the tenant use good husbandry or good farming practices on the leased property (*Commonwealth v. Peterman*, 1938). Good husbandry practices conserve the fertility, usefulness, and value of the soil (Hamilton, 1990). For example, suppose a tenant is using leased property for vegetable production and uses tillage practices that cause soil erosion and loss of soil fertility. Under this example, the tenant would not meet the good husbandry practices requirement. But if the tenant is using proper tillage practices and follows a nutrient management plan on the leased property, then the duty requiring good

husbandry practices is fulfilled. Both parties should consider clearly defining in the lease what will be considered good farming practices to limit potential disputes down the road.

## Repairs

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A question often arises as to who is responsible for repairs or maintenance required in keeping up the rented property. Traditionally in Pennsylvania, a landlord has no legal duty to make repairs to the rented property (*Hoy v. Holt*, 1879). A tenant, on the other hand, traditionally was only required to make ordinary repairs to the leased property (*Hoy v. Holt*, 1879). Ordinary repairs are those necessary to keep the leased property in working condition. Under this traditional view, a landlord would not be required to make any repairs to a leased property during the life of a lease and a tenant would only be required to make those repairs necessary to keep the leased property in working condition—all at the tenant’s own expense.

This traditional view can be altered by the lease agreement. The landlord and tenant can specify the types of repairs the landlord will be required to make, and the level of maintenance required of the tenant. For example, a lease could specify that the landlord is required to replace broken fences, and that the tenant is required to keep all roads passable. The lease agreement could also specify how the tenant be compensated for necessary repairs, such as whether the tenant receives a rent deduction for making repairs, or whether the landlord is required to provide supplies for repairs and the tenant contributes the labor.

## Entry during the Lease Period

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One big issue that can arise is when the landlord (or someone on the landlord’s behalf) may or may not enter on the leased property. Both tenants and landlords should work to clearly define the situations when a landlord can enter the leased property. This right of entry could be limited to reasonable times when the

landlord wishes to view tillage operations, planting, or harvesting. Tenants may want to allow landlord reasonable times to enter the property to make repairs. At the same time, landlords may want to preserve rights to the property for occasional recreational use such as hunting, fishing, or hiking.

One consideration for both parties in the lease termination process is allowing new tenants on the property after harvest but before the current lease has terminated. This will allow a new tenant to begin tillage or fertilizing prior to the existing lease terminating. Many landlords may want such a provision included in any lease to smooth the transition between tenants. Although landlords and tenants may not realize it when entering into a lease, leases may terminate with both parties upset with each other. Including a provision up front allowing new tenants the right to enter under limited situations is one good way to address and ease the situation, especially if both the current tenant and landlord are not communicating.

## Insurance

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Both parties will want to carry liability insurance on the leased property. This is good business practice and will protect both landlord and tenant from possible liability claims. The landlord will want to carry insurance on all structures located on the leased property to protect against loss. The tenant will want to carry insurance on his own personal property, such as tools and equipment, located on the leased property.

Crop insurance coverage will depend on the type of lease the landlord and tenant share. If a fixed cash rent lease or a flex rent lease is used, the tenant will be responsible for insuring the crop. A landlord may want to include a clause in the lease to ensure that the tenant carries a minimum level of crop insurance coverage to ensure the tenant can pay the rent. Use of a crop share lease will require the landlord and tenant to split the cost of crop insurance coverage based on the percentage of the crop owned by each party. With a custom farming contract, the landowner will need to insure the entire crop.

## Failure to Pay Rent

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Pennsylvania law allows for all a tenant's non-exempt personal property on the leased property to be sold to recover unpaid rent (68 P. S. § 250.302). The property must be that of the tenant, the tenant must be behind in payment of rent, and the lease must have ended and terminated (68 P. S. § 250.302). This can include growing crops. Property to be sold must be appraised and sold at a sheriff's sale (68 P. S. Ann. §§ 250.308–250.309). If the lease has not terminated and the tenant is not paying rent, then the landlord would have to go through a judicial process to gain the right to sell tenant's personal property on the leased premises in order to collect unpaid rent.

A process for failure to pay rent should be included when developing the lease. The process should include specific language addressing when rent is considered late (is it late after 1 day, or after 1 month?). Both landlords and tenants may want to include language requiring mediation or arbitration to settle these disputes. In many cases, use of mediation or arbitration can resolve disputes more quickly than the court system.

## Rental Fees

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What to charge or pay for rented land involves many variables. Many times a landlord will hear what the tenant is paying for other land leases, and feel they should charge a higher fee. The fees the producer can afford depend on several factors. These include, but are not limited to:

- Distance from the home farm
- The amount of land within the lease and the size and shape of the fields
- Previous use of the land
- Soil type, structure, and topography
- Access to irrigation or rights to water

The closer a producer is to their home farm or base has a direct bearing on the value of the land. Moving farming equipment over public roads takes time and agricultural tires are not designed for road use. They

will wear out much quicker when traveling on paved roads. If the producer needs to travel several miles with their equipment, the land may not be as valuable to the producer. For example, having 100 contiguous acres to rent is more appealing to agronomic crop producers than 20 to 30 acres, unless the land borders other rented land. For a horticultural crop producer, 10 to 20 acres may be ideal if there is access to water for irrigation.

For someone planning an organic production strategy, the previous use of the land is critical. To become certified organic, the land can have only approved pesticides used for a period of 3 years. If the producer must produce organically for 3 years before becoming certified, the land may not be nearly as valuable as land where no unapproved pesticides were previously used.

Knowing the soil type, structure, and topography may impact the potential rental value. If the topography is sloping enough that the land is only suitable for grazing, the rent will not be as high as more level land potentially suitable for horticultural crop production.

Communication between landlord and tenant regarding rental fees is critical to successful long-term relations. If either party is dissatisfied with the other's performance, talking through the issues can result in both parties agreeing to terms, thus preserving the relationship.

## Purchasing Agricultural Real Estate

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The purchase of farm land is a long-run decision that affects both the solvency and liquidity of your business. Because it is such an important decision, you should consider the following when you think about buying a particular parcel of land:

1. Assess the value of the property you are thinking about purchasing and its income generating potential. This should include an assessment of potential markets, cost of production, soils, topography, and climate.
2. What are the number, size, and condition of any buildings on the property? How useful are they to

the enterprises you wish to undertake? If you are considering a livestock enterprise, are there adequate handling facilities and what is the condition of the fencing? If there is a house, is it suitable for your purposes?

3. The size of a particular parcel has a large impact on its purchase price. Smaller farms generally sell for much more per acre than larger farms because more people would be able to purchase such a property.
4. Proximity to markets is a very important consideration because it affects transportation costs and potential access to consumers.
5. Because most people buying farms will also live on them, it is important to consider the community you will be living in and access to quality services including schools, shopping, medical care, agricultural input suppliers, and other infrastructure (including roads, bridges, telecommunications, and Internet services).
6. Are there competing uses for the land? If the property is near recreational or urban areas or if it contains valuable natural resources, the property will generally cost more due to these other potential uses.

When deciding to go from leasing to buying farmland, you should first sit down with your lender or financial advisor to determine if you have the financial resources and projected cash flow to support buying the property. You may want to request the last few years of the seller's Schedule F to get an idea of the costs and revenues to help you and your accountant get an idea of how profitable the land actually is.

The second thing to do would be to find a quality real estate agent who deals regularly with agricultural property. They will be knowledgeable about what you need to consider when purchasing farmland, will have an idea of what to expect, will be less stressed in the process, and will catch things you might not notice. In some situations you may not need the real estate agent to help find farm land; the property you want to buy may become available and you just need to know the process to follow to purchase the property on your own.

Thirdly, do your homework. Does the property



have the soils to support your proposed operation? Be sure to visit the local Natural Resources Conservation Office to look at the county soil survey to review the soil types on the property (or go online to [websoilsurvey.sc.egov.usda.gov/App/HomePage.htm](http://websoilsurvey.sc.egov.usda.gov/App/HomePage.htm)). You also need to determine if there are there use restrictions that impact your use of the property. Visit the local planning and zoning office to find out if zoning regulations allow your proposed farming practices and any value-added production and sales you want to pursue. The zoning office should also know if the property is enrolled in a land preservation program. Next, visit the local soil conservation district to find out if current or previous owners have enrolled part or all of the land in a state or federal conservation program that may impose temporary restrictions on the land.

Finally, you need to consider if the property matches your goals for the farming operation you envision and the needs of your family. What kind of neighbors will you have? Is the property in a good location for you (near your home or near the market you hope to supply)? Does the property have access to water?

Once you have considered these and other questions you might have, hire an experienced title attorney to review the property's title. This is not a step you will be able to skip or even attempt to do on your own. You will need someone who has checked the title to determine what temporary or permanent land uses easements, rights-of-ways, or other restrictions/limitations could exist on the property. You will want to know if the property has clear right-of-access and if a neighbor has an easement to use the property to access their own property. You will want to know if a drainage easement crosses the property, or if a conservation easement exists that could limit how you can use the property. Never rely on the seller to tell you what restrictions exist. Your lender may require title insurance and they will stipulate the depth of the search. If you are not borrowing funds to purchase the land and you still desire title insurance, you can determine the depth of the search. A good title attorney will search the chain of title (all the deeds, easements,

and other restrictions that would have been granted by previous owners). A good title attorney will be able to tell you if the current owner also owns the mineral rights, or if a previous owner has retained ownership.

You should also get an appraisal of the property, to help you know how much to offer for the property. Once you have the appraisal and are ready to make an offer, begin working with your attorney on terms you want to include in the purchase contract. Will you need the seller to make certain repairs? Will fences need to be fixed, or a barn, or some other fixture? Clearly define what stays on the property when you buy it, especially if equipment on the property is also supposed to be part of the deal.

If your offer and any additional requirements are accepted by the buyer, then you will close on the property. Working with an attorney will help ensure that the proper closing documents are prepared, such as the deeds, any state-required documents, mortgage documents, loan note, and the like. Once all the documents are signed, notarized, and the deeds filed with the county, then the sale is complete and you are the proud owner of your own farmland.



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*Hoy v. Holt*, 91 Pa. 88 (Pa. 1872).

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*Swanson v. Carlson*, 364 Pa. Super. 161 (Pa. Super. Ct. 1987).

## For More Information

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Ag Lease 101 (sample leasing agreements)  
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USDA National Agricultural Statistics Service (NASS)  
Cash Rent Survey Results  
[www.nass.usda.gov/Surveys/Guide\\_to\\_NASS\\_Surveys/Cash\\_Rents\\_by\\_County/index.asp](http://www.nass.usda.gov/Surveys/Guide_to_NASS_Surveys/Cash_Rents_by_County/index.asp)

# Sample Termination Letter

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Date: \_\_\_\_\_

To: \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

You are being given notice of an intent to terminate the lease on agricultural property described as:

\_\_\_\_\_  
\_\_\_\_\_

\_\_\_\_\_. This tenancy will terminate on the first day of \_\_\_\_\_, 20 \_\_\_\_.  
You will therefore take notice to govern yourself accordingly.

Sincerely,

\_\_\_\_\_  
Print Name

\_\_\_\_\_  
Signature



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