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Farm Property
Its Ownership and Control

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Landowners are really only stewards of the land for the period of time they own and control it. Because others are affected by the way in which private land is used, society has deemed it desirable to enforce certain rules and regulations on land use.

A landowner may maintain ownership without direct use of the land by leasing it out to one or more tenants. In this way he has the advantage that comes from increasing land values plus his share of whatever income is generated by regular farm production.

Many forms of farm business organization are available to the farm operator, whether he is an owner or a tenant. The most common are sole proprietorship, partnership and corporation. The best form of ownership for an individual farmer is one that can best help him achieve his established goals. Each farm needs to be studied on its own merits before the best type of business organization can be determined.

This publication discusses the three forms of business organization — sole proprietorship, partnership and corporation — and their use on farms, and examines land tenure changes, farm size and farm real estate values in a general way. The purpose is to provide an overview of farmland tenure and some options for operation and control of the farm business.

Farm Real Estate

Real estate is usually considered to consist of physical land together with permanent improvements which would typically be included in a sale of real property. These improvements include items such as buildings, fences, irrigation structures and drainage facilities. In some circumstances, growing crops may also be included. Livestock, machinery, commodities in storage and movable buildings are not usually considered to be part of the real estate.

Farm real estate costs make up a large proportion of the total cost of producing farm commodities. These costs include interest payments, property tax on the real estate, insurance and perhaps maintenance costs. When real estate is leased, the landlord pays these expenses but the tenant bears them indirectly in the form of rent.

Ownership in real estate consists of a "bundle" of rights pertaining to the use of property. The highest type of ownership in real estate in the United States is fee simple. It consists of an exclusive right to use the property subject to rights held by society in all property.

Rights held by the public in all real estate include police power, taxation and eminent domain. Police power is the right to enforce laws and regulations established by society. Among these regulations are zoning ordinances, building codes and rules affecting the health and safety of the public. Society's power to tax real estate places an obligation on the owner of the property directly or the renter indirectly. Eminent domain allows the compulsory purchase of land when this is deemed to be in the public interest.

The remaining rights can be exercised in any manner chosen by the owner. He may sell, lease, give easements, bequeath or handle in a number of different ways.

Farm Real Estate Ownership

The Census Bureau classifies farm ownership into three tenure categories: full owner, part owner and tenant. The full owner owns or is buying all of the farm real estate he operates. The part owner rents land in addition to his own farm real estate and the tenant leases all of the farmland he operates. Table 1 gives farm numbers, acreages and percentages in each category for Idaho. Note that part owners had 28% of the farms but controlled 57% of the farming land in Idaho in the 1974 census year.

Acquiring Farm Real Estate

You acquire land for farming purposes two primary ways. The most common is purchase or inheritance; the second is leasing. Those who are short on financial resources may be better able to get an economical farm base by leasing rather than by purchase. Income generated from the land may be inadequate to pay the full land cost at today's prices. Many land purchases have been financed by off-farm sources or by income from previously held land such as in the case of farm expansion.

Land prices have risen rapidly during the 1970's. Average increases in Idaho (Fig. 1) have been similar to those for the rest of the nation. Real estate prices in 1978 were 300% of 1967, averaging about $450 per acre.[1] Average farm size has been expanding since the early 1900's (Fig. 2). Farm technology has enabled the farmer to handle the expanding acreage by replacing labor and animal power with machines and chemicals. The expanding farm size together with the rapid increase in value per acre has greatly increased the amount of capital needed to own and operate a farm. In addition to this, interest rates have also increased.

Another way to consider land prices is in terms of commodities instead of dollars. For example, suppose a wheat farm cost $200 per acre when wheat was worth $1 a bushel and $400 when the price of wheat was $2.50 per bushel. The land value increased in dollars but decreased in terms of bushels of wheat — from 200 bushels to 160.

[1]USDA. ERS Real Estate Market Developments.

Table 1. Number and percentage of farms, average acreage and percentage of land in farms, Idaho, 1974.

Class	Number of farms	Average acreage	Percentage: Farms	Percentage: Land in farms
Full owner	14,609	332	62	34
Part owner	6,755	1,214	28	57
Tenant	2,316	527	10	9
All farms	23,680	603	100	100

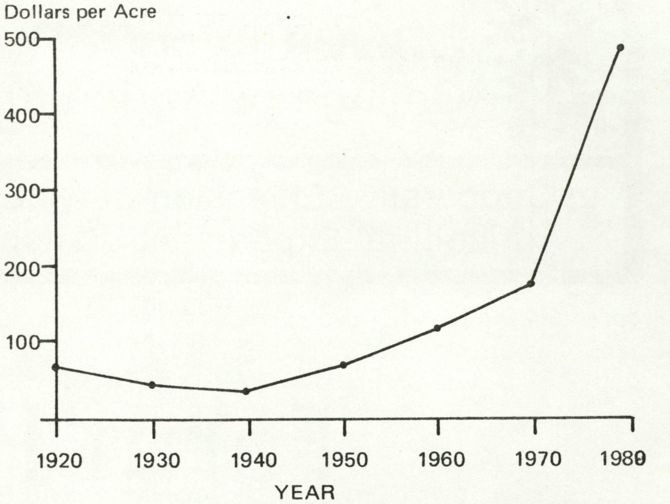

Fig. 1. Average farm real estate values per acre, Idaho, 1920-1978.

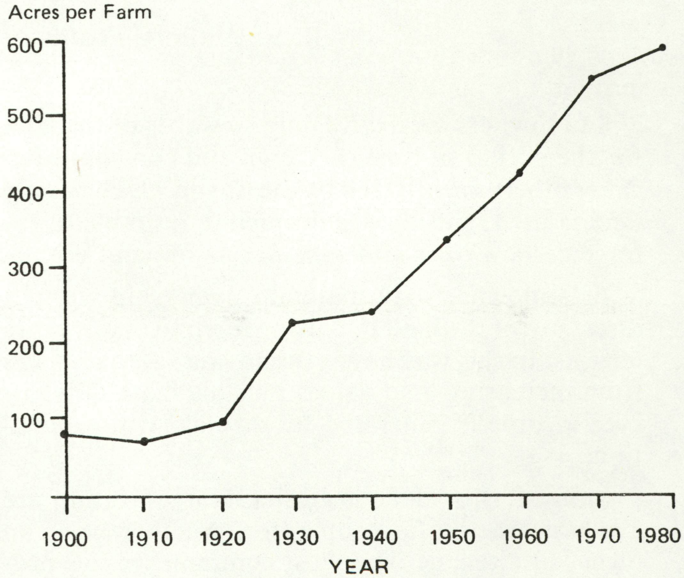

Fig. 2. Average acres per farm, Idaho, 1900-1978.

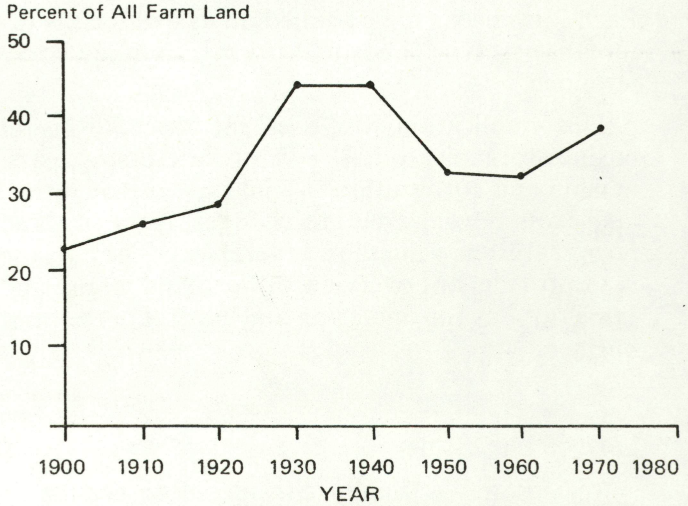

Fig. 3. Proportion of farmland operated under lease in the United States, census years, 1900-1974.

Table 2 shows the long-term relationships between average land prices and two Idaho commodities, wheat and potatoes. The table illustrates the general relationships and shows general differences from year to year. During the early 1960's, about 65 bushels of wheat equaled the value of an average acre of real estate. From 1975 to 1978, about 150 bushels of wheat were needed, because land prices increased and wheat prices declined after 1973. Similar changes are evident in the relationship of potatoes to land values. These relationships reinforce the idea that there is a demand for land as an inflation hedge or as for speculative purposes in addition to its demand for agricultural production.

Leasing Land for Farming

Leasing adds one more level of complication to the farm operation. In some ways leasing is similar to partnership, since two or more parties are obtaining income from a piece of property. The landlord temporarily transfers his rights to the use of property to the tenant. The tenant pays rent for the use of these rights to the property. Usually management decisions are a combined effort on the part of the landlord and the tenant. Each must consider the concerns of the other when making plans that affect the use of the property.

Table 2. Average price per acre of real estate and quantities of wheat and potatoes having equal value, Idaho, 1940-1978.

Year	Average real estate price per acre	Quantity equal in value to one acre of real estate	
		wheat	potatoes
	(dollars)	(bushels)	(hundred pounds)
1940	33	57	132
1950	70	38	82
1960	112	67	61
1961	114	64	109
1962	120	63	81
1963	124	67	80
1964	129	101	40
1965	134	104	69
1966	142	93	85
1967	152	115	94
1968	162	141	69
1969	168	134	83
1970	177	128	92
1971	188	141	118
1972	205	107	84
1973	229	52	59
1974	287	72	76
1975	339	100	91
1976	368	157	131
1977	412	170	153
1978	445	162	188

Another way that leasing is like a partnership is that both parties are contributing to a common production system. The landlord provides the real estate and perhaps some capital while the tenant provides labor, machinery and most of the productive variable inputs. Returns are shared on the basis of contribution. Both parties benefit when a lease is put together properly and works the way it should.

In the United States, leasing has been an important institution in farming. Fig. 3 shows the proportion of farmland rented for census years between 1900 and 1974. The low for that period was 1900 with 23% of the land rented and the high was 45% in 1935. In 1974, 35% of the land was operated by tenants. Rented acreage in Idaho has ranged from 8% in 1900 to a high of 37% in 1935. About 33% of Idaho's farmland was reported to be rented in the 1974 Census of Agriculture.

Farm Organization

The farm can be organized into one or more types regardless of whether it is a full owner, part owner or a tenant farm. The three most common types of organization are sole proprietorship, partnership and corporation. In the 1974 census, 88% of Idaho farms were classified as sole proprietorships, 8% as partnerships and 4% as corporations. Sole proprietorships controlled 74% of the cropland and partnerships and corporations each controlled 13% of the cropland. Partnerships and corporation farms averaged considerably larger acreage than the sole proprietorship farms.

The sole proprietorship is a one-person (or family) operation. The sole proprietor controls the business, makes management decisions, gets all of the income and is responsible for all debts and claims against the business. The proprietor's liability is unlimited, which means that all of his assets, whether farm-related or not, could be taken to settle a legal claim. The sole proprietorship is a flexible arrangement with very few restrictions on management decisions.

The partnership is a joint-ownership arrangement between two or more individuals. The regular partnership is very much like the sole proprietorship except that two or more decision makers bear the responsibility. Except for limited partners, liability of each of the partners is unlimited. Each partner must be compatible and have a good deal of confidence in each other if the partnership is to function well.

A limited partner usually does not make management decisions and his liability is limited to his investment in the partnership. His interest in the business is likely to be investment and he has no desire to become involved with the day to day decisions.

Advantages of a partnership arrangement include the following:

1. Resources of two or more persons can be pooled, often resulting in greater efficiency.
2. Management may be improved when the thinking of more than one person is pooled.
3. Opportunity exists for a division of labor. Each partner may specialize in a different phase of the business, thus obtaining better control than is likely with a sole proprietorship.
4. The ability to obtain credit may be enhanced by the greater resources of the partners combined.
5. The partnership pays no income tax. Each partner pays on his share of the earnings of the business.
6. A partnership is more flexible than a corporation in that fewer controls are imposed upon it.

Disadvantages of a partnership are:

1. Liability of the regular partner is unlimited.
2. Length of the partnership agreement is uncertain as it can be terminated by any partner or is dissolved on death of one of the partners.
3. When termination becomes necessary, the value of each partner's interest is often difficult to determine.
4. Personal differences are magnified and conflict between partners may arise.

The corporation has been gaining popularity as a means of organizing farm ownership in recent years. The corporation is recognized by law as an individual entity. As such it is taxable, is liable for its debts and may earn an income.

The corporation is governed by a board of directors elected by the stockholders. The corporation is organized by permission from the state. It must be properly organized, have articles of incorporation and pay filing fees. The corporation must operate under the appropriate state laws which require the holding of an annual meeting, keeping and filing minutes and election of officers.

Probably the main reasons for incorporating the family farm are:

1. Limited liability on equity capital.
2. Continuous existence.
3. Estate planning.
4. Possible tax advantages.
5. To facilitate the use of fringe benefits such as retirement plans, health insurance, etc.

Some possible disadvantages of incorporating the farm are:

1. Reduced flexibility in operating and management decisions.
2. Double taxation. (This can be avoided if the farm is organized as a sub-chapter S corporation. These corporations are taxed much like a partnership with each stockholder paying taxes on his or her share of the earnings. However, sub-chapter S corporations must meet rather rigid requirements in order to avoid the double taxation aspects of corporations.)
3. Requirement of more records and rules.
4. It may be difficult to dissolve the corporation if the owners decide some other form of ownership would be more desirable.

No matter what form of ownership is chosen, professional advice should be obtained before it is established. Qualified attorneys and accountants will be able to help with plans so that the organization is sound for tax purposes, legal protection of the owners and for estate planning purposes. A little extra planning and organizing in the beginning can reduce or prevent many problems at a later time.

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