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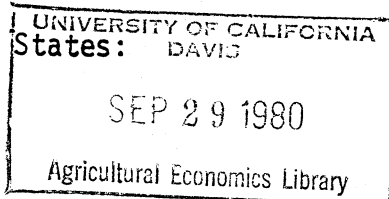
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Land Ownership Restrictions of the Midwestern
Influence on Farm Structure

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Proponents of the family farm have recently been successful in getting some legislatures of midwestern states to pass laws that restrict the rights of aliens and corporations to control farm land (Morse et al., p. 61). These laws are not the first to limit aliens in their rights to own real estate (Zagaris, pp. 38-39). For example, the common law rule in England prior to 1870 prevented aliens from acquiring good title to land without the King's approval (Blackstone, Vol. 2, pp. 249-250). The reason for limiting rights of aliens made sense in the feudal system that existed when the common law rule arose. In that feudal system, the King granted land to lords (and the lords in turn granted land to lesser lords) in exchange for a commitment to furnish specified goods or services--including service in the King's army. An alien was likely to not have the necessary loyalty to the King to uphold his obligation to provide such services. Therefore, in order to reduce the risk of conveying land to a party who would fail to perform the services promised, the law eliminated aliens (except those approved by the King) from the class of people that could hold land. The logic behind the current interest in restricting land ownership is not so simple.

The primary objective of current laws that restrict the ownership of farm land by aliens and corporations is to influence farm structure^{1/} by preserving the family farm (Minn. Stat. Ann. §500.24 (1) (Supp. 1979); S.D. Compiled Laws Ann. §47-9A-1 (Supp. 1979); Neb. Rev. Stat. §76-1501 (1976)). There are important legal and practical limitations to the effectiveness of restrictive laws in attaining that objective. Some of those limitations are discussed in the second part of this article. The first part of this article summarizes the laws of the midwestern states that restrict the rights of aliens and corporations to control farm land.

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I. LAND OWNERSHIP RESTRICTIONS

DEFINITIONS

The following are definitions of some key terms as used in this article.

A "family farm" is a farming unit that is owned and operated by people who are closely related by blood and/or marriage. A corporation, or any other business entity, will be included in the term "family farm" as long as the entity is primarily engaged in farming and is controlled by the members of a family. The characteristic that most clearly distinguishes a family farm from other farms is that the members of the family have management control. That characteristic would be seen by most proponents of the family farm as an essential element without which many of the benefits of family farms would be lost. Another characteristic that distinguishes most family farms is that the majority, if not all, of the labor is performed by members of the family. While this characteristic is probably not as universally important to proponents of the family farm as the management characteristic, many people would be less favorable to protecting a farm where more than one-half of the labor was supplied by non-family members than to protecting farms on which family members provided most or all of the labor. The final characteristic that sometimes distinguishes a family farm is ownership of the farm land by the family. This characteristic is less common and would probably be viewed by most proponents of the family farm as not an essential element as long as the family farmer is assured of the availability of land to farm. To be sure, ownership is a critical element to some proponents without which there is no point to protecting the family farm. However, most proponents would probably list land ownership after family labor and family management as the characteristics of family farms which are most important to preserve.

"Corporations" will include corporations formed under the laws of any jurisdiction for the purpose of making a profit except those that are included in "family farms" as defined above.

"Aliens" will include only those people who are not United States citizens and who live outside the United States. Therefore, "resident" aliens--citizens of other countries who live in the United States--are not included in the term "aliens."

LAWS OF MIDWESTERN STATES

The restrictive laws enacted by the legislatures of the midwestern states are quite diverse in their approach to restricting corporate and alien ownership of farm land. The following summary of the laws of thirteen midwestern states is intended only to give the reader an idea of the types of restrictions that are being used. Morrison and Krause, and more recently, Morse et al. have thoroughly compiled and discussed the restrictive laws of all the states.

The following table shows that eight of the states whose statutes were examined directly prohibit corporate ownership of farm land and ten states either prohibit alien ownership of farm land or limit the amount aliens can own. Six states include businesses controlled by aliens in their prohibitions. Four states prohibit leasing farm land by aliens and corporations and seven states prohibit corporations from engaging in farming.

The exceptions to those restrictions are too numerous and varied among the states to be cataloged here. A few examples will be illustrative. The most common exception is for corporate ownership and use of farm land for research, production of seed stock or similar activities. Some states allow corporations or aliens who owned land on the effective date of the law to retain the land they owned and in some cases to acquire more land to accommodate a reasonable rate of growth. Most of the states provide a period of time for an alien or corporation to divest land they are prohibited from owning or to become eligible to own the land.

In addition to the above restrictions, seven of the states require corporations, aliens and alien controlled businesses that are legally

Summary of Laws of Thirteen Midwestern States
Restricting Agricultural Land Ownership

Key to reading table:

1. A "C" indicates the state has a law that applies to all corporations except family farm corporations unless otherwise noted.
2. An "A" indicates the state has a law that applies to non-resident aliens unless otherwise noted.
3. An "AB" indicates the state has a law that applies to businesses that are controlled by non-resident aliens.

Laws	Prohibits Owning Agricultural Land ^{a/}	Prohibits Leasing Agricultural Land	Limits Amount of Agricultural Land that can be owned	Prohibits Farming	Requires Reports ^{b/}
States					
Illinois	<u>A^{c/}</u>				
Indiana			<u>A^{c/}</u> (320 A.)		
Iowa	C, A, AB	C			<u>C^{d/}</u> , A, AB
Kansas				C	
Michigan					
Minnesota	C, A, AB			C	<u>C^{d/}</u> , A, AB
Missouri	C, A, AB	<u>A^{e/}</u>		C	<u>C^{d/}</u> , A, AB
Nebraska	<u>C^{f/}</u> , <u>A^{c/}</u> , AB				<u>C^{d/}</u>
North Dakota	<u>C^{d/}</u> , A, AB			<u>C^{d/}</u>	A, AB
Ohio					A, AB
Oklahoma	<u>C^{g/}</u> , A	<u>C^{g/}</u>		<u>C^{g/}</u>	
South Dakota	C	C	A (160 A.)	C	<u>C^{d/}</u> , <u>A^{h/}</u>
Wisconsin	C		A, AB (640 A.)	C	

^{a/}There are a myriad of minor exceptions to the general prohibitions in the various states such as a divestment period, grandfather clauses, experimental uses and others.

^{b/}These reports are required of entities owning agricultural land and are in addition to annual corporate reports which are required by all of the states.

^{c/}Resident aliens are subject to the law.

^{d/}Family farm corporations are also subject to the law.

^{e/}Law applies only to lease for more than ten years.

^{f/}Law applies to all corporations that are incorporated under jurisdictions other than Nebraska (including family farm corporations) but does not apply to any corporations that are incorporated in Nebraska. Nebraska corporations cannot be controlled by aliens.

^{g/}Family farm corporations that are incorporated under jurisdictions other than Oklahoma are subject to the law.

^{h/}South Dakota just monitors reports required by the federal Agriculture Foreign Investment Disclosure Act of 1978.

holding agricultural land to file an annual report detailing the background of the owners and their use of the property.

II. LIMITATIONS OF THE LAWS

LEGAL LIMITATIONS

The major legal limitations on the states' restrictive laws are the federal constitution and international treaties (Morrison, p. 639). Morrison concludes that state laws which restrict the rights of resident aliens (e.g. Illinois, Indiana and Nebraska) are less likely to survive a constitutional attack under the equal protection and due process clauses of the fourteenth amendment than laws which restrict the rights of non-resident aliens and corporations.

The reason for that distinction is that land ownership for a resident alien is a basic need similar to welfare benefits, employment by the state and eligibility for a profession which the United States supreme court has held cannot be withheld on the basis of alienage. By contrast, non-resident aliens and corporations do not have the same basic need to own American land and therefore can constitutionally be discriminated against if the state can show a "rational relationship" between those classifications and a legitimate state interest (Morrison, pp. 642-643).

There is a rational relationship between the two classifications (aliens and corporations) and the law's purpose of influencing the local economy. However, the state has a legitimate interest in influencing the local economy only if the federal powers over foreign relations and foreign commerce (U.S. Constitution Article I, §8) do not pre-empt the states' powers in those areas. Morrison concludes that the simple exercise of mechanical rules (such as the exclusion of aliens from ownership of land) has not been pre-empted by federal foreign relations activity (p. 649). Nor has the federal government pre-empted the foreign commerce field since it has ratified treaties which presume the validity of state legislation

restricting the ownership of real estate (p. 652). Therefore, state laws restricting resident alien's ownership of farm land are very likely to be held unconstitutional if tested in the courts, but such an attack would not invalidate the portion of the restrictive laws that limit the rights of non-resident aliens and corporations.

Treaties entered into by the United States are a part of the "supreme law of the land" (U.S. Consitution Article VI, Paragraph 2) and thus override inconsistent state legislation. Many of the existing treaties grant rights to conduct business and to acquire land necessary for the operation of the permitted business. However, most treaties reserve the right to limit or exclude alien activity in exploitation of land which, if exercised, would validate restrictions on alien ownership of farm land. Furthermore, the treaties often expressly recognize the laws of states regarding their land. Therefore, state laws restricting alien ownership of farm land are likely to be consistent with treaties and not overridden by them.

PRACTICAL LIMITATIONS

Having determined that state laws restricting the rights of aliens and corporations are likely to be legally effective, some of the practical limitations which reduce their effectiveness will be examined.

Legal Avoidance and Illegal Evasion. Laws restricting alien ownership of farm land can be legally avoided if aliens are not also prohibited from owning a controlling interest in a trust or business that owns farm land. Even if an alien is legally forbidden to own farm land indirectly, the law is difficult to enforce if several layers of corporations or fiduciaries are used to hide the identity of the beneficial owner. The same problem arises if a corporation is the beneficial owner of farm land. Iowa has attempted to solve this problem by requiring all conveyances of agricultural land (including leases for a period of five years or more) to be recorded and the beneficial ownership of such conveyances to be disclosed

(Morse et al., p. 109). Zumbach and Harl discuss the limitations on a state's ability to pry information out of corporations that are incorporated under the laws of other states. They conclude that a federal reporting system (such as the Agriculture Foreign Investment Disclosure Act of 1978) would be more effective in penetrating the layers of corporations and fiduciaries to determine the beneficial owner (pp. 325-331).

Supply of Family Farmers. Proponents of the restrictive laws are likely to think that the income of family farmers will be increased by the laws as well as the number of family farms. They probably reason that the restrictive laws will reduce the price of land and therefore increase the net income to family farmers which is the remainder of the revenue from farm products after the costs of all farm inputs are subtracted. The ability of restrictions on farm land ownership to raise the income of family farmers depends upon the elasticity of supply of family farmers.

It is reasonable to assume that the elasticity of supply of family farmers is quite high for the following reason. There is an annual flow of farm youth from midwest farms to full-time off-farm jobs (Abourezk, p. 500). Because of this flow, the farm sector would not have to attract people from other lines of work in order to increase the number of family farmers but simply retain some of the youth who have grown up on farms and would otherwise leave the farms (Johnson, p. 182). These youth, already trained to operate a farm, are likely to be very responsive to an increase in net farm income.^{2/} The high elasticity of supply of family farmers means there will be a large increase in the number of family farmers as a result of a small increase in the net income of family farmers. The retention of youth that would otherwise have left the farm will continue until their competition for the net income from farming has driven that

net income back to the level where farm youth at the margin would again be indifferent between leaving or staying on the farm.

The form which the competition among the farm youth would take is in bidding for the other factors of farm production until the costs of the other factors rise to the point that net income is reduced to the level stated above. Therefore, if the elasticity of supply of family farmers is high, barring or limiting alien and corporate purchase of farm land will have little effect on the net income of family farmers.

Motives of Alien Investors. The restrictive laws may also be less effective than expected because the threat to the family farm is less than expected. While this is not a limitation of the laws themselves, it should be considered with the other limitations so that the effect of the laws is not over stated. The issue is whether the motives of alien investors are compatible with family farming.

Before analyzing that issue, I will delineate and discuss two factors that affect the current market value of farmland--the flow of income from the land and its expected value in the future.^{3/} Those two factors are not independent since future value depends upon the expected flow of income in the future which is correlated to the current flow of income. Despite their lack of independence, the two factors will be treated separately in this analysis since they provide independent reasons for purchasing farmland. The flow of income will be referred to as the productive value of farm land and the expected future value will be referred to as the speculative value of farm land.

The productive value and the speculative value of a given piece of land do not necessarily have to be owned by the same entity. For example, an investor could purchase fee title to farm land and lease it on a long

term basis to a farmer. The rental rate would reflect the land's productive value while the purchase price would reflect the total of the land's productive, speculative and other values. The investor could sell the speculative interest at any time by selling his fee title subject to the rights of the farmer as lessor. The farmer could sell the productive value at any time by assigning the lease to another party. Therefore, for a given piece of land, its speculative and productive values can be severed from each other, transferred from one party to another and recombined as the supply of and demand for them dictates.

The argument that aliens and corporations push farm land prices high enough to bar new family farmers from entering the industry implies that both the total price of land is too high and that the cost of severing the productive value from the speculative value is also too high. However, the transfer cost of acquiring the productive value of land from an investor who is only interested in the speculative value should not be prohibitive. The only parties involved in the transaction are the farmer and the investor. The investor will be concerned that the quality of the land is not diminished by the farmer's overuse or lack of care of the land. That problem could be dealt with in a two-party contract by stating a standard of use and care which the farmer must comply with or be liable for the resulting damages. The farmer will be concerned about having the right to farm the land for a period long enough to justify investing in equipment to farm the land.^{4/} As the length of the agreement is increased, the farmer will acquire more of the speculative value since he or she will acquire the right to more of the future production on which the speculative value is based. Arriving at an agreeable length of time should not be an insurmountable problem, however, because the investor's time horizon is likely to be as long or longer than the period necessary to justify

the farmer's investment in equipment.^{5/} Furthermore, both parties can reserve the right to transfer their interest in the land to a third party.

Perhaps potential new farmers would choose not to farm if they were not assured of having their land to farm for the period required to justify their investment in machinery. While the risk of having to find new land to lease or to change careers if their lease were not renewed would certainly reduce the attractiveness of farming, it would surely not be an absolute bar to farming since most of the alternative careers available to potential farmers have some (if not more) risk of being unavailable within the same period of time. For example, the changing supply of and demand for construction workers, engineers or lawyers could force people in any of those careers to find employment in a different location or a different occupation.

The severability of the productive and speculative values of farm land is important in analyzing the compatibility of alien investment and family farming. To the extent aliens purchase land as an investment and not as a means of acquiring the commodity produced on the land,^{6/} they will be interested only in maximizing the return on their investment. Since aliens by definition do not reside in the United States and therefore cannot farm the land personally, their alternatives for realizing the productive value of their land are to (1) manage the farms themselves or by an agent and hire the necessary labor to farm the land, (2) rent the land on a crop share basis or (3) rent the land for cash. Given the investor's distance from the land, a cash lease would be the least expensive to supervise and for that reason may be the most attractive alternative. If the alien investor does choose to lease the land for cash and is willing to lease it for the period of time necessary to justify the investment in machinery, the alien investor is very little threat to the family farm. A crop share lease takes some of the management away from the family farmer but for most of the proponents of the family farm, it

of the family farm, it probably leaves enough management with the family to satisfy the desire to preserve the family farm. Therefore, if the alien investor rents the land either for cash or a share of the crop, the fact that the land is owned by an alien rather than the family farmer or another American has little effect on the existence of the family farm.^{7/}

If the alien investor chooses to manage the farm and hire the necessary labor, the management of the farm would be severed from the labor to such an extent that most proponents of the family farm would probably consider the essential characteristic of the family farm to have been lost. Therefore, if a sufficient amount of land is purchased by alien investors and if a sufficient portion of them manage their land directly, then alien investors would pose a threat to the family farm. The portion of American farm land which alien investors must own and manage to be a serious threat to the family farm is subject to debate. Some ownership and management of farm land by aliens is likely to be compatible with family farming since working on an alien investor's farm may supplement the income of young family farmers during the years when they have more labor than can be effectively employed by their own capital and management.

Therefore, to the extent alien investors in American farm land are interested only in the return on their investment and do not manage the farm themselves or by an agent, they will have little effect on family farms. Consequently, the main effect of laws restricting alien investors in farm land would be to allow the family farmer to be an investor in farm land as well as a farmer. As Atkinson and Jone suggest (p. 62), with the increase in the size of farms, the assumption that the ownership and operation of family farms must be in one entity may no longer be valid.

CONCLUSION

There are some important limitations on the effectiveness of restrictive land ownership laws in preserving the family farm. Restrictions on resident

aliens' right are likely to be unconstitutional under the equal protection clause. The rights of non-resident aliens and corporations do not receive the same level of constitutional protection. Therefore, restrictions on the rights of non-resident aliens and corporations to own farm land are likely to survive a constitutional attack. While international treaties override inconsistent state law, state restrictions on farm land ownership are likely to be consistent with existing treaties and therefore valid.

Aliens can legally avoid restrictive laws if they are not prohibited from owning farmland indirectly through corporations or fiduciaries. Enforcement of laws prohibiting indirect ownership is difficult on the state level because of the states' limited right to pry information out of corporations organized under the laws of another state. If the elasticity of supply of family farmers is high, the restrictive laws will have very little effect on the level of income of family farmers. Finally, to the extent alien investors are not interested in acquiring the commodity from the farm land and are not interested in managing the farm, they pose very little threat to the family farm. If the threat of alien investors to family farms is low, then laws restricting alien investments will do little to protect the family farm.

These limitations of the restrictive laws can be explored more thoroughly as data become available from the various reporting laws. The limitations may prove to be so great that the benefits of the restrictive laws do not justify their cost.

Footnotes

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1. The term "farm structure" is used in this article to refer to the characteristics of the entity engaged in farming such as its size, the role of families in operating the farm and the role of the farm entity in the surrounding community.

2. Johnson cites (on pp. 186-187) a study by Edward W. Tyrczniewicz and G. Edward Schuh of Purdue University which estimated the long-run elasticity of supply of unpaid family farm workers to be -3.26.

3. There are other factors that affect the value of farm land such as its amenity value, expected inflation and others. Harris and Hampel have developed a model which uses nine variables to determine the bid price of farm land. The other factors do not affect this analysis and are therefore not delineated here.

4. The average useful life of farm machinery is a good first approximation of the length of that period of time. While there are well developed markets for used machinery, the transaction costs of buying and selling make the costs of buying and selling on a yearly basis prohibitive.

5. The alien investor who is willing to pay the transaction costs of investing in American farm land is likely to be interested in holding that investment for at least the useful life of the farmer's machinery.

6. Currie et al. found no desire among the foreign investors in Iowa farm land they surveyed to acquire the commodities from the land for foreign consumption (p. 129).

7. Currie et. al. found in all their observations that local residents continued to operate the land after it was purchased by foreign investors. The USDA reports (p. 22) that at least 67 percent of the farm land in the United States reported as acquired by foreign investors between February 2, 1979, and May 31, 1979, had no change in tenure as a result of the purchase. The land on which a tenure change did occur could, of course, be a change from one local tenant to another.

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