

Understanding Ag Contracts

ERIN HERBOLD-SWALWELL, JD, IOWA FARM BUREAU
FEDERATION

DECEMBER 21, 2023



We encounter contracts every day

Farm Leases

Solar, Electric,
Wind or Pipeline
Easements and
Options

Custom Farming
Agreements

Agreements
regarding farm
data

Fencing
Agreements

Drainage
Agreements

Subcontractor
Agreements

Real Estate
Installment
Contracts

Purchase
Agreements

Threshold Question

- ▶ Legacy- will the next generation be impacted by entering into this agreement?
- ▶ Are you interested in entering into the contract?
 - ▶ Does it align with your values?
 - ▶ Who are the parties?
 - ▶ What is the motivation to enter into the contract?
 - ▶ Is there room for negotiation?

The Art of Negotiation



Assessing what is most important to you



What can you give up? What is non-negotiable



Negotiating as a group might be more effective, especially with one-sided contracts

Read the contract



Insurance policies/contracts- livestock operations and grain



Crop insurance



Premarital Agreements- Requirement for meaningful opportunity to consult with an attorney- examples with farm families

The Building Blocks of a Good Contract

Mutual Assent- Each party is of a like mind

Offer and Acceptance- needs to be clear, defined terms

Consideration- Each party to a contract receives something of value in exchange for goods, service or payment

Performance or delivery

Good faith- each party making an honest commitment to follow terms

Why a written document? Let's look at farm leases

- ▶ The Statute of Frauds- some statutes require that certain contracts are memorialized in writing and signed by the party against whom they are to be enforced against
- ▶ i.e. Farm Leases
 - ▶ Only 2/3rds (according to recent data) are in writing
 - ▶ Provides a clear record of agreement, especially in the event of subsequent disagreement or litigation (what is admissible in litigation?)
 - ▶ Clears up tax issues
 - ▶ Succession of farm lease
 - ▶ Encourages discussion on important issues
 - ▶ Lease supplements- tile and drainage improvements

What every farm lease should have...



Accurate property description



Each contract has a beginning and end-termination



Amount of rent paid and when



Signatures- who are the parties?



Use of property- (who has possession) i.e. hunting, storks



Good stewardship language



Wealth of forms available



Cash rent vs. Hybrid/Flex lease vs. Crop share

Farm Leasing and Business Relationships

- ▶ Sometimes the hardest part of renegotiating a lease is approaching the landlord and starting the conversation. Many landlords and tenants have worked together for many years and have the same goal in mind- the continuity and stability of their farming operation. The following are some tips and ideas to keep in mind when approaching your landlord:
 - ▶ Suggest a different arrangement
 - ▶ Negotiate a long-term lease at a reasonable rate, spreading the risk between landlord and tenant, and “locking-in” a fair rate over the long-term.

Other thoughts

If you are a “beginning farmer,” educate the landowner on the financial/tax incentives available

Propose an Investment in Conservation Measures in lieu of extra cash rent.

Retired farmer tax planning: Farm Lease Income Exclusion or Iowa Capital Gain Deduction?

Flexible Leasing

Approximately 12% of cash leases in Iowa are now flex leases (Maybe more)

Advantages

- Shared risk
- Owners still paid cash
- Actual rent adjusts with adjustment in yields and prices
- Options for flex leasing:
 - Share of gross revenue
 - Base rent plus a bonus

Lease drafting: Commonly left out provisions

Hunting clause

- Implied covenant of quiet enjoyment

Recreational Use

- *Sallee v. Stewart*

Crop Residue

- Section 562.5A effective July 1, 2010

Ensuring Payment

- ▶ Landlord has right to receive rent promised by tenant
 - ▶ *McElwee v. DeVault*
 - ▶ However, tenant must be given opportunity to cure

Iowa Landlord's Lien

- ▶ Iowa Code Ch. 570
- ▶ Landlord must file financing statement to perfect
- ▶ Within 20 days after debtor takes possession of leased premises
- ▶ Payment up front?
 - ▶ \$5 filing fee
 - ▶ File anyway?

Farm Lease Termination

- ▶ Iowa Code Section 562.5: “In the case of a farm tenancy, the notice must fix the termination of the farm tenancy to take place on the first day of March, except in cases of a mere cropper, whose farm tenancy shall terminate when the crop is harvested.”

Amendments to Iowa Code Section 562.6

- ▶ *If an agreement is made fixing the time of the termination of a tenancy, ~~whether in writing or not~~, the tenancy shall terminate at the time agreed upon, without notice. Except for a farm tenant who is a mere cropper, a farm tenancy with an acreage of forty acres or more shall continue beyond the agreed term for the following crop year....*

Termination date

- ▶ *Foster v. Schwickerath*: Wrong termination date of Dec. 31 did not nullify the notice and notice of termination was valid for a termination date of March 1, since notice was served prior to Sept. 1

Farm leasing

- ▶ Common situation: “As a tenant, I didn’t terminate my 2023 cash rent lease because I didn’t think the landlord would renegotiate and I didn’t want to lose the land. Banker is telling me I need to lower the cash rent.”
- ▶ Sept. 1 termination applies to all tenancies except animal feeding operations (even under 40 acres)

Farm lease termination and estates

Common situation: Landlord has a good relationship with tenant. Landlord does not terminate the farm lease, however, landlord and tenant renegotiate the lease each December. What happens if the landlord dies?

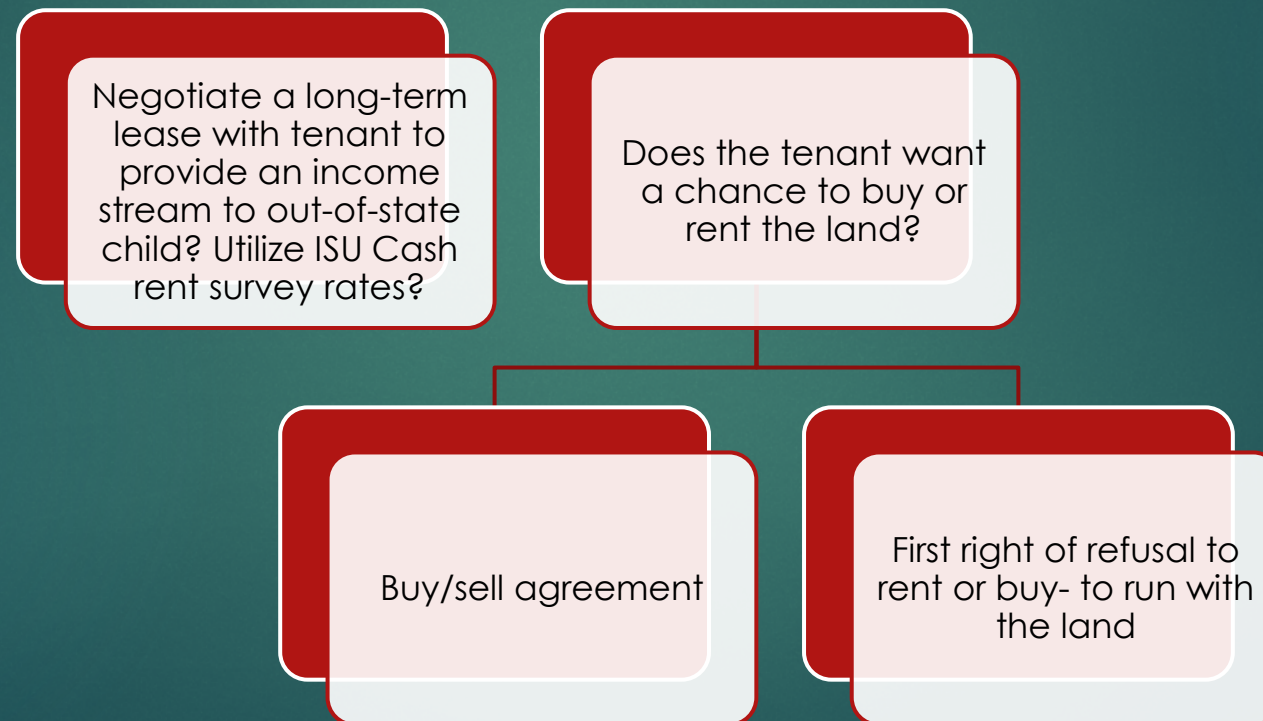
Sept. 1 termination applies to all tenancies except animal feeding operations

Developing a long-term leasing plan may help avoid this situation

Case study #1:

- Facts:
 - Landlord is 80 years old and has one child who lives out of state.
 - Child does not plan to move back to Iowa and would prefer a gift of cash when Landlord dies
 - Landlord has leased the land to a neighbor for many years and the neighbor has expressed an interest in maintaining that relationship.
 - Neighbor's daughter is coming back to the farming operation

What are the landlord's options when planning?

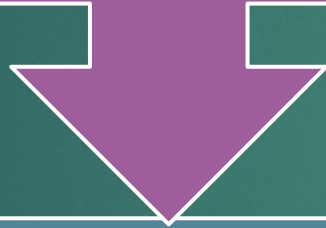




Contract Issues in Business relationships and entities

WHAT TO LOOK FOR

While it is relatively “cheap” to set up an entity, you will want to make sure you put together a plan for operating the entity and examine the goals of the operation with your trusted advisors.



Drafting a good operating agreement is key to the success of this arrangement and the operation of the entity, especially if others are involved in the operation.

Business
Entities: The
importance
of an
operating
agreement-
a contract
or roadmap
for
members

Buy/Sell Agreements are contracts

- ▶ What other tools are available to us? Buy-sell agreements, option agreements, machinery sharing agreements will help insure that your heirs are able to purchase or inherit the tools, equipment, or other assets they need to carry on the operation.
- ▶ Helpful tool in contracting with on-farm heirs to start the process of transfer of assets during life
- ▶ Machinery, land, other equipment
- ▶ Life insurance to assist?
- ▶ Get it in writing



Benefits of a Funded Buy-Sell Agreement



Creates a guaranteed Buyer for your business interest

Ensures your family gets paid a fair price – preserves the value of your business

Negotiate price and terms when all parties on equal footing

Assures the continuity of your business enterprise as a going concern

Insurance- Property and Casualty

Make sure farm liability insurance covers your unique situation.

An *insurance policy* is a contract between the policy holder and the insurance company. The coverage provided depends upon the terms of the insurance policy.

Read and understand the policy and have an advisor review the policy carefully. In doing this review, be sure to explain to the agent or other advisor, as much as possible, what your operation looks like.

You may also consider getting an individual written coverage opinion from the insurance company if you have special circumstances, such as regularly hosting farm tours.

How to read your policy



What activities are actually covered under your policy? Maybe the more important question is, what is not covered under your policy.



A standard farm liability coverage policy will contain a list of items that are not covered. For instance, custom farming might not be covered or other non-farm activities such as excavation



Again, ask yourself, what unique risks are present in my farming operation.



Who is covered under your policy? A major question to ask is whether coverage extends to your all of your family member, employees, and their representatives. In other words, who are the insured parties?

Planning for the unknown

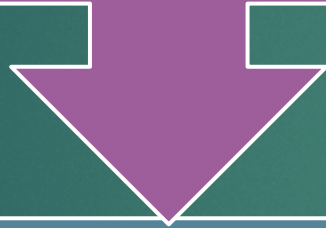


While we cannot predict what the future holds for the farming operation, we can manage risk by looking at farm liability policies as risk management tools.



You may want to run some “hypothetical” situations by your insurance agent, and see what coverage would or would not apply.

What coverage amount should I have? What is the aggregate limit of the policy? With increased land values and increased risk, it may be necessary to investigate more coverage.



Take a look at your balance sheet with your insurance agent and other trusted professionals and ask whether your current coverage limit would protect the current value of your farm.

How much coverage?

Insurance Contracts

You may want to run some “hypothetical” situations by your insurance agent and see what coverage would or would not apply.

Release forms are contracts

- Are release forms or liability waivers a good idea? While this is another step in liability protection, waivers offer limited protection. Due to another recent Iowa Supreme Court case, a release signed by a parent of a minor child on a field trip does not apply to the child.
- Waivers can offer protection for liability claims by adult visitors but any waiver should be prepared by an attorney for each individual situation.

What about our data? Protecting ourselves with contracts

- ▶ Big Data: Who owns it? Who controls it? Data is intangible, not a physical good like our raw commodities. The waters are muddy
 - ▶ Farm data, as we know it today, consists of agronomic data (soil nutrient levels, yields, application levels, etc.), machine and computer data, and weather data relating to the climate in a particular area.
 - ▶ Farm data is unique because it “can be tied to geospatial information.” In other words, farmers can now pinpoint the exact yield in every area of their fields.
 - ▶ There are two big areas of concern from a legal standpoint with respect to farm data- protecting the privacy of farm data and protecting the ownership of farm data.
 - ▶ Is the law of trade secrets the only real path for the protection of farm data in our *existing legal framework*? The Uniform Trade Secrets Act, adopted in Iowa, defines a “trade secret” as “information ... that derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by a person able to obtain economic value from its disclosure or use and is the subject of efforts to maintain its secrecy.”

Protect your data

- ▶ Negotiate up front
- ▶ The owner of the data needs to take steps to protect that data and maintain its secrecy.
 - ▶ For instance, in a farm lease situation, one may want to include language granting the tenant the rights to the data on the leased farmland until the conclusion of the lease. Following the termination of the lease, the farm data must be transferred back to the landowner or the subsequent tenant.
- ▶ Custom farming arrangements? If a local co-op sprays pesticides on your field, who owns the data that generates?
- ▶ Does access to farm data impact farm rental rates? Over the long term and as our use of farm data grows, we may see that historical data and its ownership may enter into leasing negotiations.

Easements or leases: Wind, solar, electric line, pipelines

- ▶ i.e. New “solar collector farm” (photovoltaic) projects proposed. Landowners contacted, asking to enter into long-term leasing agreements/easements

Common questions:

- ▶ What if the company runs into financial problems, declares bankruptcy, and walks away from these solar installations?
- ▶ Are these companies dependent on a government subsidy or tax credit to make the project work? Is the use compatible with my farming operation and where will transmission lines be installed?
- ▶ What incentives (i.e. government subsidies) are available to these companies?
- ▶ In the event of financial distress, what will the company do to ensure that I am paid?

What is the difference between leasing land and entering into an easement?

- ▶ Remember, a lease is really just a contract where the party owning land gives the other party the right of control over what is leased. A landowner can't interfere with the rights of the tenant during the period of the lease. It does not transfer legal possession
- ▶ An easement is a similar concept. Gives limited rights to use a part of the landowner's properties. For instance, utility companies generally request easements for utility line installations.

List of important questions to ask – leases, options and easements:

- ▶ What is the term of the agreement? How many years? Are there options to renew after the initial term expires?
- ▶ Is the agreement assignable? (Can the company assign their rights to another company?)
- ▶ What is the payment and how is it structured?
- ▶ Am I protected from liability as a landowner, if a catastrophic event occurs?
- ▶ What access rights, and through what routes, does the company have? If the company damages my crops or compacts my soil, what does the agreement provide for compensation?
- ▶ In the event of a legal dispute, is there a mandatory arbitration or mediation clause? Do I have to give up my right to a trial by jury?

Easements or Leases

1

Stay informed-
go to meetings

2

Negotiate as a
group if you
can

3

Review the
agreement with
your attorney

Agreements with the County, IDOT, etc.

- ▶ Landowners are often approached by their county governments with easements or offers to purchase small portions of land for the improvement of highways, bridges, or other infrastructure.
- ▶ What to look for?
 - ▶ What is the compensation and how is that determined?
 - ▶ What is the purpose?
 - ▶ How long will it take?
 - ▶ Will this interfere with farming practices?

Fence agreements, drainage agreements



A quick update



A good agreement will “run with the land” and avoids later confusion if land transfers or is sold

Real Estate Contracts and Purchase Agreements



CONSULT YOUR
ACCOUNTANT



WHAT IS THE TERM,
DOWN PAYMENT?



WHERE IS THE
ABSTRACT?



DO I NEED AN
APPRAISAL?

Any questions?

- ▶ Erin Herbold-Swalwell
- ▶ 515-226-6538
- ▶ Erin.Herbold-Swalwell@fbfs.com