Chapter IV. Other Land Transfer Tools

Introduction
The transfer of farmland to a successor often happens by will or gift. It can also entail the purchase of the farm by the successor or successors. The materials that follow discuss two legal tools that can facilitate purchase by a successor. Land contracts are a seller financing mechanism that can be especially useful for successors unable to obtain commercial credit. They are not without risks, however. Cooperative land ownership can ease affordability for a successor willing to farm cooperatively with others. It may be especially useful for a group of employees who want to purchase the farm from their employer and operate as a cooperative.

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I. Land Contracts for the Transfer of Farmland

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A land contract is a long-term executory contract for the sale of land. The buyer agrees to make regular principal and interest payments, usually annually, to the seller. The seller of the land agrees to transfer title to the buyer once all payments have been made. The buyer takes possession when the contract is first entered.

A land contract can provide an exiting farmer with a seemingly simple means of transferring farmland to a family or non-family member. Payments provided in installments can ease the tax consequences for the recognition of gain on the sale. A new farmer unable to obtain commercial credit can obtain possession of land without a significant down payment. An exiting farmer can also retain a life estate in the homestead on the farm.

There are risks, however. Default, waste, a decline in land values, and bankruptcy of the buyer are all risks to the seller. The buyer, too, risks forfeiting possession and all payments made if a payment is missed. This may be why many land contracts are executed between parents and their children rather than between unrelated parties.

A. Risk of Default, Risk of Forfeiture

Some buyers are ineligible for commercial or FSA lending. A land contract can offer an alternative, seller-financed route to land ownership. Because the seller is taking on the significant risk of default, a land contract almost always will provide that if the buyer defaults on a payment, he forfeits possession of the property and all the payments made to date. This "forfeiture clause" is sometimes considered a form of liquidated damages. As a measure of liquidated damages, it can become unreasonable where the buyer has made most of the contract payments and made significant improvements to the farm prior to default.

Treatment and enforcement of a forfeiture clause vary a great deal by jurisdiction. Some states will enforce a forfeiture clause but require that the seller provide a brief right to cure and a right of redemption upon full payment of the contract. (For example, this is the approach taken by statute in Maine.) Some courts have adopted a restitution theory requiring a seller to return any payments to the extent that they exceed the seller's actual damages. Some of these states will use a rental value theory of damages, others will look at the fair market value of the land at the time of default in relation to the contract price. (For example, market value is used to determine reasonable damages in land contract cases in New Hampshire). Also see Freedman v. Rector 230 P 2d 629 (Cal. 1951).

The Restatement of Property §3.4(a) (1997) takes the position that a land contract should be regarded as a mortgage with the seller's remedy being foreclosure. If the property sells foreclosure for more than the contract price, the buyer gets the excess. If the property sells at foreclosure for less than the contract price the seller has a right to the deficiency. In this way, the seller gets the benefit of his bargain. Several states have adopted this approach. See Skendzel v. Marshal 301 N.E 2d 641 (Ind. 1973) and Kubany v. Woods, 622 So. 2d 22 (Fla. Dist. Ct. App. 1993)

The treatment of forfeiture provisions in New England jurisdictions are as varied as the rest of the country. And in several jurisdictions, there is little to no guidance on whether a forfeiture clause will be enforced.

Maine:

Maine has adopted a Land Contract statute for any contract for the sale of real estate requiring at least 5 or more installment payments exclusive of a down payment. 33 M.R.S. §481.2

The statute includes a detailed list of required land contract provisions including the following:

K. A statement which explains that the contract is not a mortgage and that the purchaser does not obtain title to the property until the purchase price is paid in full.

L. A statement of the rights of the buyer established by Title 14, §6111 to cure a default by the buyer.

14 M.R.S.§6111.1, however, only provides a right to cure in the case of "residential property located in the state when the mortgagor is occupying all or a portion of the property as the mortgagor's primary residence and the mortgage secures a loan for personal, family or household use…"

33 M.R.S.§6203-F the state's foreclosure statute also provides a right to cure, right of redemption and an opportunity to extend the right of redemption for up to one year for a foreclosure upon a bond for deed or for contracts for the sale of real estate. This provision, however, also only applies to residential real estate.

In Thurston v. Galvin, 2014 ME 76, 94 A 3d 16(2014), the court considered whether a seller under a land contract in default was entitled to a writ of possession or if instead the property was to be sold at the expiration of the redemption period as dictated by the mortgage foreclosure statutes. The court said:

In land installment contracts generally, and certainly in this one, the purchaser's contractual rights are limited to possession of the premises until she has made the final payment. [5] The vendor retains legal title to the property. See Thompson v. Skowhegan Sav. Bank, 433 A.2d 434, 436 (Me. 1981) (stating that " the vendor of land under an installment sale contract retains legal title to the land"). Accordingly, because Galvin's sole rights are possessory rights, those are the only rights affected by the section 6203-F foreclosure process. Ending Galvin's right to possess the property, but then compelling the Thurstons to submit the property to a public sale would implicate the vendors' rights in the property, rather than the purchaser's rights. The plain meaning of section 6203-F precludes such an interpretation. Here, the only applicable provisions of 14 M.R.S. § § 6321-6325 are those that apply to Galvin's right to possess to the property, i.e., those provisions that concern Galvin's rights of redemption. As to those, there is no dispute.

We recognize that a growing number of courts have held that a land installment contract should be treated as a mortgage, at least in those cases where the purchaser's payments have been more than nominal, so as to afford a purchaser rights beyond redemption. See Restatement (Third) of Property: Mortgages § 3.4 cmt. b(3) & reporters' note (1997) (compiling cases); Grant S. Nelson, The Contract for Deed As A Mortgage: The Case for the Restatement Approach, 1998 BYU L. Rev. 1111, 1115-16 & n.58. We note, however, that the contract between Galvin and the Thurstons contains no language suggesting that Galvin should be permitted to recoup any of the payments made before breaching the contract. In addition, our treatment of a land installment contract as a mortgage would render meaningless the words " the rights of the purchaser in the contract" in section 6203-F. This we cannot do. See Blue Yonder, LLC v. State Tax Assessor, 2011 ME 49, ¶ 13, 17 A.3d 667 (" [W]e must not interpret the statutes in a manner that would render some of the language superfluous and meaningless.”). To alter the statutory protections enjoyed by a purchaser of land through a land installment contract " is the province of the Legislature, not of this Court." Mason v. Town of Readfield, 1998 ME 201, ¶ 8, 715 A.2d 179. Thurston at 21.

Vermont

The only case in Vermont to mention Land Contracts stands for the proposition that a breach of a land contract does not create the relationship of a landlord / tenant or render the buyer subject to the summary ejectment procedures available under landlord tenant law. The court does make the statement that land contracts are “regarded in equity as analogous to equitable mortgages.” Strengowski v. Gomes 128 Vt. 555, 268 A. 2d 749 (1970)

Dicta in full: *Contracts of this character, contemplating the purchaser's use and occupancy of the premises, are regarded in equity as analogous to equitable mortgages. The right of forfeiture or defeasance for a breach of the covenants contained in the contract was only in aid of the security. Van Dyke and Drew v. Cole, 81 Vt. 379, 396, 397, 70 A. 593. Strengowski at 750.*

New Hampshire

In Newcomb v. Ray, 99 N.H. 463(1955) the court ordered restitution to a defaulting buyer under a land contract reasoning as follows:

In the hands of the defendants, the part payments made by the plaintiffs represent a net benefit to the defendants to the extent that, when added to the net amount actually received by the defendants from the sale of the property, they exceed the net amount which the defendants would have received from the property if the plaintiffs had completed the purchase of it. Omitting consideration of the legal expenses of $84.10, an item chargeable to the defendants in any event upon the sale of the property, the net amount which the defendants would have received if the plaintiffs had completed their purchase would have been $29,700, the purchase price of $33,000 less the real estate commission of $3,300. On the same basis, the net amount actually received from the sale of the property was $24,700, the sale price of $26,000 less the real estate commission of $1,300. The net amount of $24,700 actually received by the defendants from the sale plus the net amount of $6,700 received by them from the plaintiffs totals $31,400. The net benefit to the defendants is the difference between this total and the $29,700 which they would have received had the plaintiffs performed the contract. The plaintiffs are entitled to that part of $1,700 which is 'in excess of the harm' caused to the defendants by the plaintiffs' breach of the contract. (emphasis supplied)

Similarly, in Randall v. Riel, 123 N.H. 757 (1983) the court remanded a forfeiture case saying:

At the hearing on remand, reasonable damages should be determined as the difference between the market value of the property and the contract price, plus such other special damages as may have resulted from the plaintiff's breach of the contract for deed. Cf. Bower v. Davis & Symonds Lumber Co., 119 N.H. 605, 609, 406 A.2d 119, 122 (1979) ($10,000 liquidated damages provision was reasonable because property was sold in an arms-length transaction after breach for $90,000, which was less than $100,000 contract price).

Massachusetts

In Cameron v. Gunstock Acres, Inc., 370 Mass 378 (1976) the court notes:

A purchaser under an instalment land contract resembles a mortgagor in some respects. Barrell v. Britton, 244 Mass. 273, 278--279, 138 N.E. 579 (1923). But the plaintiff does not tell us what rights he claims under the law of New Hampshire, which would seem to control any mortgage analogy. Cf. Churchill v. Bigelow, 333 Mass. 196, 198, 129 N.E.2d 903 (1955).

Rhode Island

There is no case law or statutory provisions on land contracts in Rhode Island.

Connecticut

La Fleur v. Pohronezny, WWMCV064003658S the Superior Court of Connecticut upheld a forfeiture provision in a bond for deed, characterizing it as a valid liquidated damages clause, saying:

"Enforcement of liquidated damages clause is subject to well established legal criteria. First, Connecticut recognizes the right of parties to agree to liquidated damages in the form of forfeiture of a deposit or a portion thereof for breach of an agreement to purchase real estate." Willert v. Russo, Superior Court, judicial district Danbury, Docket No. CV 07 5002983 (May 4, 2009, Sommer, J.). Second, a liquidated damage clause in a contract will be upheld if the following requisite conditions are met: "(1) The damage which was to be expected as a result of a breach of the contract was uncertain in amount or difficult to prove; (2) there was an intent on the part of the parties to liquidate damages in advance; and (3) the amount stipulated was reasonable in the sense that it was not greatly disproportionate to the amount of the damage which, as the parties looked forward, seemed to be the presumable loss which would be sustained by the contractee in the event of a breach of the contract." (Citation omitted; Internal quotation marks omitted.) Bellemare v. Wachovia Mortgage Corp., 284 Conn. 193, 203, 931 A.2d 916(2007). "The party seeking to repudiate a clause that fixes a sum as damages has the burden of showing that the agreed upon sum is so exorbitant as to be in the nature of a penalty." Syncsort, Inc. v. Indata Services, 14 Conn.App. 481, 485, 541 A.2d 543, cert. denied, 209 Conn. 804, 548 A.2d 443 (1988).

And later:

The court finds based on the evidence before it that the damage to the plaintiff is uncertain and difficult to prove. Additionally, as evidenced by the presence of the liquidated damages clause in the bond for deed, it is clear that the parties intended to liquidate damages. Finally, the forfeiture of the defendants' interests in the property and the sums paid prior to the breach is reasonable and not disproportionate to what the presumptive amount of damages would have been in the event of breach. Accordingly, the court orders that any interest the defendants have in the property and all moneys paid under the bond for deed be forfeited.

B. FSA Land Contract Guarantee Program

Land contracts involve risks for both buyers and sellers. Default, waste, a decline in land values, and bankruptcy of the buyer are all risks to the seller. The buyer, too, risks forfeiting possession and all payments made if a payment is missed.

A new Land Contract Guarantee Program included in the 2014 farm bill could help mitigate some of the risks of land contracts, at least for sellers. How a buyer will fare in the event of default even with an FSA guarantee is still very much a function of each state's treatment of land contracts.

FSA defines a land contract as follows: An installment contract executed between a buyer and a seller for the sale of real property, in which complete fee title ownership of the property is not transferred until all payments under the contract have been made. 7 C.F.R. §761.2(b)

FSA offers two types of land contract guarantees.

1. Prompt payment guarantee will guarantee payment of an amount not to exceed three amortized annual payments, plus real estate taxes and insurance for the period covered by the annual installment.

2. The standard guarantee program will guarantee an amount equal to 90% of the outstanding principal under the land contract. Outstanding principal is calculated as the outstanding balance less the liquidated or appraised value of the real estate.

Eligibility

1. Buyer must be a beginning (BF) or socially disadvantaged farmer or rancher (SDFR.) 7 C.F.R. §763.5(b)(1)

A beginning farmer will not have operated a farm for more than 10 years. If an entity, all members must meet this definition. The BF must materially and substantially participate in the operation. Must not own farmland or owns farm property which does not exceed 30 percent of the average farm acreage of the farms in the county where the property is located determined from the most recent Census of Agriculture. The BF must demonstrate that available resources of the BF and spouse are insufficient to enable the BF to enter or continue farming on a viable scale. 7 C.F.R. §761.2(b)

A socially disadvantaged farmer or rancher is a member of a group whose members have been subject to racial, ethnic or gender prejudice because of their identity as members of a group without regard to their individual qualities. These groups consist of American Indians or Alaskan Natives, Asians, Black or African Americans, Native Hawaiians or other Pacific Islanders, Hispanics, and women. For an entity, the majority interest must be held by SDFR individuals. For married couples, the SDFR individual must have at least a 50% ownership interest in the farm business and make most of the management decisions, contribute a significant amount of labor and generally be recognized as the operator of the farm. 7 C.F.R. §761.2(b)

2. Buyer must be the owner and operator of a “family farm” after the contract is completed. 7 C.F.R. §763.5(b)(2)

A family farm is defined as a business that produced agricultural commodities for sale in sufficient quantities so that it is recognized as a farm rather than a rural residence; where the majority of day-to-day physical labor and operational and management decisions are made by the borrower and persons related to the borrower by blood or marriage or in the case of an entity, the members responsible for operating the farm. The farm may use reasonable amounts of temporary labor for seasonal peak workload periods. 7 C.F.R. §761.2(b)

3. Farming Experience

Buyer must have participated in the business operations of the farm for at least 3 years out of the last 10. One year of postsecondary agriculture courses may count toward the 3-year requirement. 7 C.F.R. §763.5(b)(3)

4. Citizenship Status

The buyer and in the case of an entity, all members must be citizens of the United States or be a qualified alien under the applicable Federal immigration laws. A qualified alien includes anyone who is lawfully admitted for permanent residence under the Immigration and Nationality Act. 8 U.S.C §1641 and 7 C.F.R. §763.5(b)(7)

5. Credit History

The buyer must have an acceptable credit history demonstrating satisfactory debt repayment. A history of failure to pay will demonstrate an unacceptable credit history but not isolated instances of late payments or a lack of a credit history.

Limitations

The purchase price of the farm may not exceed the lessor of $500,000 or the current fair market value of the property. Existing land contracts are not eligible for the program. A guarantee may not be used to establish or support non-eligible enterprises. 7 C.F.R. §763.6

Feasibility

The buyers proposed operation must be feasible. Projected income, expenses and production estimates must be based on the buyer's last three production cycles. For those farming less than 3 years, a combination of actual history and other reliable sources may be used. When a feasible plan depends on income from sources other than farming, the income must be dependable and likely to continue. 7 C.F.R. §763.10

Contract Terms and Modifications

The buyer must provide a minimum down payment of five percent of the purchase price of the farm. The interest rate must be a fixed rate not to exceed the Agency's direct farm ownership loan interest rate in effect at the time the guarantee is approved plus three percent. The loan must be amortized for a minimum of 20 years with equal annual installments during the term of the guarantee. Balloon payments, are prohibited during the 10 year terms of the guarantee. 7 C.F.R. §763.12

The seller and the buyer may modify the contract to lower the interest rate and the corresponding annual installments without Agency approval. With written approval from the Agency the buyer and seller may defer installments, lease or sublease, transfer and assumption and assignment provided the modification is justified by a feasible plan with reasonable projections for the upcoming operating cycle.

Prompt Payment Guarantee

Loss limits, guarantee period and conditions

1. The maximum loss amount is limited to three amortized annual installments or an amount equal to three annual installments plus taxes and insurance incurred during the period covered by the installments. 7 C.F.R §763.11(a)
2. The guarantee period shall not exceed 10 years from the effective date of the contract. 7 C.F.R §763.11(b)
3. The seller must select an escrow agent who will receive the land contract payments; notify the Agency and the seller if the buyer defaults; make a demand upon the Agency to pay the missed payment; and perform other servicing duties. 7 C.F.R. §763.18

Default

1. The escrow agent must make a written demand to the buyer for the payment of the defaulted amount within 30 days of the missed payment. 7 C.F.R §763.20(a)
2. The escrow agent must make a written demand of the Agency within 90 days from the original payment in the buyer has not covered the delinquency. 7 C.F.R §763.20(a)(1) and (2)
3. Any amount paid by the Agency as a result of an approved loss claim is immediately due and payable by the buyer. If the debt is not restructured into a payment plan the Agency may use all remedies available to collect the debt. The debt may be rescheduled for repayment consistent with the buyer's ability to pay, not to exceed 7 years. 7 C.F.R. §763.21

The Agency will cover only 3 missed payments. During this period the buyer will retain in possession of the land. If the buyer defaults the fourth time, the seller's rights will be dictated by the contract between the two parties and how that particular state treats land contracts. If the contract and state law favor forfeiture provisions, the buyer will have to vacate the property and will lose any payments made. Or state law (or the contract) could require some measure of restitution to the buyer.

Standard Guarantee Plan

a. **Guarantee period and conditions**

1. The guarantee period shall not exceed 10 years from the effective date of the contract. 7 C.F.R §763.11(b)

2. The guarantee will cover an amount not to exceed 90 percent of the outstanding principal balance. 7 C.F.R §763.11(a)(2)

3. The seller must use a third-party servicing agent approved by the Agency who will receive installment payments and send them to the seller; provide evidence to the Agency that property taxes are paid; perform an annual physical inspection of the farm; Obtain a balance sheet and income statement and cash flow on an annual basis; notify the Agency if the buyer defaults; and service the delinquent accounts. 7 C.F.R. §763.18(b)

b. Default

1. If the buyer fails to pay an annual installment then the seller has the option of either liquidating the property or having the loss amount established by the Agency by an appraisal of the real estate. 7 C.F.R. §20(b)

2. The servicing agent must make a written demand to the buyer within 30 days of the missed payment. If the payment is not made within 60 days of the demand letter the servicing agent must immediately inform the Agency whether seller will utilize the liquidation method or the appraisal method to establish the loss amount. 7 C.F.R. §20(b)(1)

    Liquidation Method:

    The servicing agent will submit a liquidation plan to the Agency and complete liquidation within 12 months of the missed payment unless prevented by bankruptcy, redemption rights, or other legal action. Credit an amount equal to the sales price received in liquidation to the principal balance of the land contract. 7 C.F.R. §20(b)(2)(i)

    Appraisal Method:

    The Agency will complete an appraisal on the real estate and the loss claim will be based on the difference between the appraised value at the time of the loss and the unpaid principal balance of the land contract. The Agency will retain a lien on the property in the amount of the loss claim. If the property sells within 5 years from the date of the loss payment the seller must repay the Agency the difference, up to the amount of the loss claim. 7 C.F.R. §20(b)(2)(ii)

3. Any amount paid by the Agency as a result of an approved loss claim is immediately due and payable by the buyer. If the debt is not restructured into a payment plan the

> Agency may use all remedies available to collect the debt. The debt may be rescheduled for repayment consistent with the buyer's ability to pay, not to exceed 7 years. 7 C.F.R. §763.21

Whichever route the seller chooses, appraisal or liquidation, FSA will ensure that the seller gets the benefit of his bargain. The buyer's rights upon default will be dictated by the terms of the contract between the parties and that state's laws on forfeiture. If forfeiture is favored, the buyer could lose all payments made under the contract. If state law provides an opportunity for some form of restitution of payments made, the buyer could exercise those rights.

C. Risk of Bankruptcy

A land contracts may extend for 10 or even 20 years. A lot can happen in that time span, including the seller or the buyer filing bankruptcy.

Debtors in Bankruptcy are allowed to "assume, assign or reject" executory contracts. If the seller is the debtor, however, the code provides certain protections to buyers under a land contract. If the buyer is in possession, the buyer has the option of terminating the contract or remaining in possession and continue to make the payments. The Bankruptcy trustee will recive payments and deliver title to the buyer when all the payments have been made. 11 U.S.C. §365.

If the buyer is the debtor there is less clarity with respect to whether the land contract will be treated as an executory contract or as a mortgage. If the latter, the seller will have a security interest in the land up to the value of the land. If the seller is undersecured, the balance of claim is treated as an unsecured debt and a large portion of it may be subject to discharge.

If the land contract is treated as an executory contract the buyer must assume, reject or assign the contract without modifying its terms or discharging any of the debt. Bankruptcy Courts will look to state law in deciding whether to characterize a land contract as a mortgage or an executory contract.

D. Elements of a Land Contract / Checklist

(Adapted from Maine's land contract statute at 33 M.R.S §482 and "Financing Farmland with an Effective Land Contract: A Toolbox" by Farm Commons.)

Land Contract Elements

1. The full names and post-office addresses of all the parties to the contract.
2. The date the contract is signed by each party.
3. A legal description of the property conveyed.
4. The sale price of the property conveyed.
5. Any charges or fees for services included in the contract separate from the sale price.
6. The amount of the buyer's down payment.
7. The principal balance owed by the buyer. Which is the sum of the sales price of the property conveyed and the amount of any charges or fees for services included in the contract separate from the sales price.

8. The amount and due date of each installment payment and the total number of installment payments.
9. The interest rate on the unpaid balance and the method of determining the interest rate.
10. Will the land contract include an acceleration clause? Will the land contract include a forfeiture provision?
11. Will the land contract provide a right to cure?
12. A statement indicating the seller has good and marketable title.
13. A promise that the seller will deliver a warranty or other type of deed upon completion of the contract.
14. Will either or both buyer and seller have a right to mortgage or assign their interest in the contract?
15. A provision that, if the seller defaults on any mortgage on the property, the buyer may pay on the mortgage and receive credit on the land installment contract.
16. A requirement that the buyer shall be responsible for the payment of taxes, assessments and other charges against the property from the date of the contract, unless agreed to the contrary.
17. A provision that the buyer has the right to accelerate or prepay any installment payments without penalty, unless agreed to the contrary.
18. A provision that states which party will be responsible for the payment of insurance and which party will be responsible for damages to the property.
19. A promise on the part of the buyer to not commit waste, damage or destruction of the property.
20. A provision that states what happens if the land is condemned or the government takes the land.
21. How and whether the land contract can be amended.
22. A force majeure provision.
23. A statement that the land contract will be recorded.

E. Alternatives to a Land Contract

There are other lease-to-own strategies that are less risky than a land contract. A long-term lease with a right of first refusal or an option to purchase can also provide a pathway to farmland ownership. A right of first refusal gives the lessee the right to match any third party offer to purchase the property. An option to purchase grants the lessee a right to purchase the property within a time frame and under the terms specified in the option. An option included in a lease may expire if the lease is terminated. An option separate from the lease will expire under its own terms. These strategies, however, are not without risk.The primary risk is that the lessee will make significant improvements to the property but is ultimately unable to exercise the option. For more on these alternative lease to own methods see the Appendix 5, Lease to Own Fact Sheet.

II. Cooperative Land Ownership

Annette Higby

In this discussion, cooperative land ownership means using the legal structure of a cooperative rather than meaning the broad concept of farming "cooperatively." Cooperative land ownership has the potential for providing affordable land access for multiple producers willing to farm cooperatively on one farm property. In the context of farm transfer, it can provide a tool for employees to purchase the farm from their employer. Or a farm in transition may be too large (and too expensive) for just one successor. Cooperative land ownership can offer one means of joint ownership. The cooperative legal structure, however, is unique – unlike more common legal structures that farmers and attorneys are more familiar with and perhaps more comfortable with.

See Appendix 1, Cooperative Legal Structure Comparison

The primary differences in the cooperative legal structure relate to:

- voting rights
- distribution of profits
- initial capital contributions, and
- the purpose of the business.

In a non-cooperative business, voting rights are usually, though not always, determined by a member's capital share in the business. In a co-op, every member has one vote regardless of their capital.

In a non-cooperative business, profits are usually though not always distributed on the basis of a member's capital share. In a cooperative, profits are returned to the members in proportion to their use of the co-op. In this way, members are encouraged to do business with the co-op rather than some other business. The return is called a "patronage dividend." In a land co-op, the patronage paid is rent, and profit is returned in proportion to the amount of rent paid by the member.

In a cooperative, the initial capital contribution is most often equal. Many state cooperative formation statutes, in fact, limit the amount of capital that can be owned by any one member. In a non-cooperative business, capital contributions can vary quite a lot.

The purpose of a non-cooperative business is to make money for its owners. The purpose of a co-op, however, is to provide goods and services to its members at cost. This is why, some state statutes refer to cooperatives as non-profits. While a co-op is a for profit venture, the profits are returned to members in proportion to their patronage.

Co-op taxation also is quite different. Co-ops can retain earnings or distribute them to members. Co-op income can be characterized as unallocated equity, or non-qualified deferred patronage which is taxed at the co-op level, or as cash distributions to members, or qualified allocated equity which is taxed at the member level. Identifying an account familiar with cooperative taxation is essential.

Co-ops also strive to operate under certain principles adopted by the International Cooperative Alliance in 1995. Some of these principles are embedded in state cooperative formation statutes.

A. Cooperative Principles

1. Voluntary and Open Membership. Cooperatives are voluntary organizations, open to all persons able to use their services and willing to accept the responsibilities of membership, without gender, social, racial, political or religious discrimination.

2. Democratic Member Control. Cooperatives are democratic organizations controlled by their members, who actively participate in setting their policies and making decisions. Men and women serving as elected representatives are accountable to the membership. In primary cooperatives members have equal voting rights (one member, one vote) and cooperatives at other levels are also organized in a democratic manner.

Each shareholder has only one vote, the earnings are distributed in a uniform dividend and one individual cannot own more than 10 percent of the capital stock.

3. Member Economic Participation. Members contribute equitably to, and democratically control, the capital of their cooperative. At least part of that capital is usually the common property of the co-operative. Members usually receive limited compensation, if any, on capital subscribed as a condition of membership. Members allocate surpluses for any or all of the following purposes: developing their co-operative, possibly by setting up reserves, part of which at least would be indivisible; benefiting members in proportion to their transactions with the co-operative; and supporting other activities approved by the membership.

4. Autonomy and Independence. Cooperatives are autonomous, self-help organizations controlled by their members. If they enter to agreements with other organizations, including governments, or raise capital from external sources, they do so on terms that ensure democratic control by their members and maintain their co-operative autonomy.

5. Education, Training and Information. Cooperatives provide education and training for their members, elected representatives, managers, and employees so they can contribute effectively to the development of their co-operatives. They inform the general public - particularly young people and opinion leaders - about the nature and benefits of co-operation.

6. Cooperation among Cooperatives. Cooperatives serve their members most effectively and strengthen the co-operative movement by working together through local, national, regional and international structures.

7. Concern for Community. Cooperatives work for the sustainable development of their communities through policies approved by their members.

B. New England Cooperative Formation Statutes

State statutes will generally provide specific formation requirements for producer marketing co-ops, consumer co-ops, worker co-ops, and credit unions. In some states, co-ops can also be formed under the general corporate formation statutes provided the entity will meet certain requirements with respect to one member one vote, payment of dividends and other cooperative principles. If there is no provision for cooperative formation under the general incorporation statue, then a land co-op would most resemble a consumer co-op as it is providing a good (land) to its members at cost although it isn't always a good fit.

Vermont

11 V.S.A. §981 and §991 et seq.

Maine

13 M.R.S. §1501

Massachusetts

Mass. Gen. Laws 157 §1 et seq.

Connecticut

Conn. Gen. Stat. §33-183, et seq.

Rhode Island

R.I. Gen. Laws §7-8-1, et seq.

New Hampshire

New Hampshire R.S.A. §301-A1, et seq.

C. Land Cooperative Examples and Case Studies

A Multi-Stakeholder Land Cooperative

A land co-op can be a single stakeholder co-op (just farmers) or multi-stakeholder. Poudre Valley Community farms in Colorado is an example of a multi-stakeholder farmland co-op. Still in the fundraising stage, members of this co-op will be consumers, restaurants, and producers. The co-op will own the land and rent it to member producers under long-term market rate leases. http://poudrevalleycommunityfarms.com/the-plan/ Patronage dividends are to be paid based on the amount of food purchased from co-op producers rather than rents paid to the co-op. The land in this example is not being offered to farmers "at cost" but at market rates. Multi-stakeholder co-ops can present significant challenges given the conflicting interests of farmers who want market and land access at cost and consumers who want high quality food at the least possible cost. In addition, most state formation statutes don't recognize or allow multi-stakeholder cooperatives. On the other hand, multi-stakeholder cooperatives provide a greater member pool for raising capital.

A Vermont Multi-Stakeholder Land Cooperative

Lost Meadow Land Cooperative holds about 600 acres of land in West Corinth, Vermont. Currently, it is used solely for residential purposes with 6 home sites. They have recently posted on Vermont Land Link, looking for a farmer member to farm 10 acres of cleared land with the potential to clear an additional 15. There is also potential home site for the new farmer member.

Ground Lease

Co-op members hold ground leases for the home sites and the area immediately surrounding the home site. The initial term is for 20 years but can be renewed for an unlimited number of additional terms. Lessees pay taxes attributable to the home site. Lessee also pays carrying charges consisting of the portion of operating costs and expenses of the co-op related to the property of which the home site is a part. In addition, Lessee pays an assessment for the cost of building and maintaining common lands of the co-op. Improvements are owned by the Lessee. The home site and improvements may not be sold without the consent of the Co-op. The ground lease is inheritable.

Bylaws

Members purchase one or more common shares at a price determined by the Co-op Council. Redemption is available only on terms as determined by the Council and only when replacement capital is available. Net profits are allocated on the basis of member patronage. One member, one vote.

The Lost Meadow Ground Lease and Bylaws can be found in the appendix.

Feasibility Case Study

Four separate farming operations explored a cooperative land ownership structure for a Vermont farm capable of supporting two diversified vegetable farms, one dairy, one beef, and one maple operation. All four farm families were then leasing the conserved premises under a single lease from the owner. In addition to serving member farms, the Co-op had the potential to rent its infrastructure and facilities to community members for events, gatherings, a farmer's market, food hub and private/commercial use. The Co-op's member marketing reach had the potential to further sales and brand awareness for the Co-op members on a regional scale.

The members agreed on a "one member, one vote" structure and that the co-op would provide land access at cost to its members. Rental payments to the Co-op and other fees for services provided would form the basis of each member's patronage. Membership was to be limited to farmers. The Co-op would have a board of directors to make decisions on land use, financials, membership, and marketing. Land use and farm management was to use holistic farm planning.

The purchase price for the farm was $574,000. Discussions with the Cooperative Fund of New England indicated that members would need to raise approximately 20% or $110,000 in the form of cash equity in order to secure the remainder as a loan. The initial capital outlay of $27,612 per member proved too steep for several of the prospective co-op members. Annual debt service financed through lease payments would have also been a challenge for several of the members. Other potential members preferred to invest their available capital into their own farming operations rather than a new cooperative. Many landowners in the area were offering short term land access for free. The operations were all at varying stages in their development and for the nascent operations the prospect of committing additional time and energy into a new entity was unappealing. Among other things, this example illustrates the importance of first doing a feasibility study before you begin to draft the by-laws and ground lease; of counseling clients on the responsibilities and time commitments required for co-op governance; and that all prospective members should be in a similar formative stage and ready to move forward with land ownership.

Well Spring Land Cooperative

Created in 1994, Wellspring consists of 189 acres in Marshfield, Vermont. The legal structure is similar to Lost Meadow although two house sites were subdivided from the 189 acres to allow the owners to obtain a mortgage. Members must own a home on the property and must reside there. In addition to the ground lease for the home sites, members enter into an agricultural lease with the co-op and pay a separate lease fee. The bylaws also deal with dissolution of the cooperative. See 8.1. of the Well Spring bylaws in Appendix 4.

Conclusions:

- Cooperative land ownership can make land access more affordable.
- Start with a feasibility study.
- If multi-stakeholder, identify and address conflicts of interest.
- Educate clients on significant differences in the cooperative legal structure and cooperative governance.
- Taxation is unique as structure; specialized tax advice is essential.
- State cooperative statutes can be arcane and a bad fit.
- Farm operations should be in a similar developmental stage and in similar economic status.
- Difficulty of obtaining a mortgage on homes and improvements.
- Consider carefully redemption and dissolution provisions.

Appendices

1. Chart: Cooperative Legal Structure Comparison
2. Lost Meadow Ground Lease
3. Lost Meadow Bylaws
4. Well Spring Land Cooperative Bylaws
5. Land for Good, Lease to Own Fact Sheet