Farm Finance Tools in Montana

2019

Overview

Access to land and capital are two of the largest problems facing today's farmers. Beginning farmers and ranchers find it increasingly difficult to find and afford farmland. Established farm families face the challenge of succession--how to finance retirement for the older generation without losing the land to development. The Community Food and Agriculture Coalition invited Trust Montana to be a partner organization for their BFRDP grant, Enhancing On Farm Success. One of Trust Montana's tasks on this project is to research community investing and land access tools, and determine whether they are viable in our state. This guide is intended to be a resource for farmers, ranchers, bankers, mortgage brokers, title companies, realtors, and investors interested in addressing affordability issues for farmers and ranchers.

Goals

1. Explain where the money for each tool comes from
2. Describe the buy-out/pay-back strategy
3. Assess the risks and benefits of each tool
4. Provide detailed models of the different tools

Table of Tools Covered in the Guide

I. Cooperatives

Agricultural cooperatives have been created in situations where farmers cannot obtain funding from investor-owned firms because the provision of these services is judged to be unprofitable by the IOFs, or the prices, terms, etc are not favorable for the farmers. Agricultural cooperatives allow farmers to pool production and/or resources, or to join forces with their communities, CSA members, distributors, anyone interested in helping them succeed. Cooperatives provide a method for members to join together in an association, through which they can reduce individual risk and acquire a better outcome, typically financial, than by going alone. This creates economies of scale which can produce a result the individual members could not achieve on their own. Cooperatives exist across a broad membership base, with some cooperatives having fewer than 20 members while others can have over 10,000 depending on the needs of the members.

While the economic benefits are a strong driver in forming cooperatives, another important strength of a cooperative is the members retain the powers of governance, ownership and control. This ensures that the profit reimbursement (either through the dividend payout or rebate) goes only to members, not shareholders of a corporation.

Cooperatives have been around since the 19th century, and for good reason: by pooling their resources, people of modest means can accomplish together what they are unable to do alone. For farmers in Montana, this means applying the state's cooperative statutes to overcome today's agricultural financial challenges. In Montana, cooperatives may capitalize their enterprises by issuing both common and preferred stock that is exempt from federal securities registration and reporting requirements. This cooperative advantage has opened up new possibilities for community investment in local agriculture and the entire local food system.

A. Land Access Cooperatives

These can be organized as small, single-stakeholder style co-ops, where all members are farmers or ranchers actively engaged in agricultural production, or they can be multi-stakeholder cooperatives (MSCs), a type of co-op that formally allows for governance by representatives of two or more "stakeholder" groups within the same organization, including consumers, producers, workers, volunteers or general community supporters. Rather than being organized around a single class of members the way that most cooperatives are, multi-stakeholder cooperatives enjoy a heterogeneous membership base.

The common mission that is the central organizing principle of a multi-stakeholder cooperative is also often more broad than the kind of mission statement needed to capture the interests of only a single stakeholder group, and will generally reflect the interdependence of interests of the multiple partners. Poudre Valley Community Farms in Colorado is an example of a multi-stakeholder co-op that purchases farmland and provides long-term tenure for farmers. The vehicle for achieving a land access coop is this: It has aspects of a traditional consumer cooperative, like a food co-op, where consumers pool their buying power to purchase products at better prices. It also has aspects of a traditional producer cooperative, like most farmers' cooperatives, that pool buying power and access to distributors and consumers to benefit the producer. The third, and MOST important, part of this cooperative model is that the consumers and the producers contribute capital through their membership dues which is used to purchase farmland. The long-term access to farmland to produce food is the key to this land cooperative model.

Cooperative developer Brianna Ewert from Lake County Cooperative Development Corporation in Ronan, Montana, presented via Skype, citing Poudre Valley Community Farms in Colorado as an excellent example of a multi-stakeholder co-op that purchases farmland to provide long-term tenure for farmers. In addition to harnessing the power of the collective to negotiate lower prices for members and increase access to distributors and consumers, what is unusual about Poudre is how it uses the capital from consumers' and producers' initial stock investments to purchase farmland—a concept that really got people talking.

B. Rural Investment Cooperatives

Janice Brown, the executive director of the Montana Cooperative Development Center in Great Falls, built upon this concept by introducing Rural Investment Cooperatives (RIC), for-profit associations whose members invest in tangible assets such as farmland, affordable housing, and historic buildings. The RIC would lease its land or equipment assets at favorable terms to increase a farmer's likelihood of success while not expecting a major return, especially over the short term. Even if they are not wealthy, member-owners can help revitalize small rural communities through their patient investment in cooperative stock.

"Although the annual return to each preferred stockholder will be modest—not exceeding the 6 percent threshold established by Montana law—the economic benefits to the community at large should be significant," said Brown.

This tool makes community investment a viable, exciting option for agricultural finance. Organic farmer Drew Blankenbaker from Lifeline Produce in Victor, Montana, having already dipped his toes in cooperative development research, made the decision at the summit to create an RIC to provide capital for farmers in the Bitterroot Valley—and just like that, the Farmland Investment Company was born. Once incorporated, this RIC will intentionally purchase farmland and offer five-year lease-to-own contracts to beginning farmers, allowing them to gain the operational experience necessary to qualify for conventional, FSA[EO1] financing.

One option for people wanting to invest in an RIC is to designate a portion of their Individual Retirement Account (IRA) funds in local farming and ranching operations. Instead of leaving employee retirement-savings investment choices to large mutual funds or an employer, an individual can specify that they want those funds to go into an RIC.

How RICs work in Montana:

- Each member-owner purchases one share of common stock and is entitled to one vote.

- Purchase of additional shares of nonvoting preferred stock is optional. Members elect a voluntary board of directors to do research into potential investments.

- Cooperative passes capital on to the farm or ranch selected by the board.

- Cooperative charges a fee for dealing with 401(k) tax and investment limit issues, due diligence, and management of funds.

- The typical co-op board is elected by member-owners; each member-owner has one vote, regardless of the size of their investment. But RICs may include multiple classes of members and investors.

C. Grassbanking

The Natural Resources Conservation Services (NRCS) defines a “Grass Bank” as a physical place where forage is made available to ranchers, at a reduced fee, in exchange for tangible conservation benefits being produced on participants’ home ranches. The main goal of grass-banking is to have a community-based conservation plan that provides meaningful benefits for both the environment and participating ranchers. Several grass banks have emerged across the U.S. Lands in grass banks can be entirely private, public, or a mix of both. Typically, grass banks are operated by a conservation organization and include a privately owned or managed base property with associated public land grazing allotments.

With rotational grazing, ranchers get higher calf weights and grow more grass that can be stockpiled for dry years, but the up-front costs such as increased labor to move cattle and fencing more frequently can be a barrier to adopting the practice. Landowners wanting to defer grazing on their land to rest the vegetation often can’t afford to on their own. Nonprofit and government-owned grass bank can help ranchers make the transition. Montana Fish, Wildlife & Parks also is on board with the practice at more than a dozen wildlife management areas (WMAs). Conservation groups including the National Audubon Society, National Wildlife Federation, and Trout Unlimited provide economic incentives for ranchers to manage cattle in ways that protect streams and native plants.

The Nature Conservancy operates a grass bank in Montana at the 60,000 acre Matador Ranch. TNC sells grazing opportunities to ranchers if the ranchers agree to adopt conservation practices on their private ranch land. The conservation practices a ranch has to adopt vary based on the specific landscape of that property. Examples include protecting sagebrush cover or maintaining prairie dog habitat. Ranchers can get up to 50% discount on grazing rights at the Matador if they comply with the agreement. Ranchers in the program who turn existing prairie into cropland on their ranch are permanently disqualified. According to Brian Martin, providing grazing rights on the Matador has increased rancher awareness of the benefits of cooperative efforts, beyond just working with nonprofits and WFP. He sees participants in the program also engaging directly with neighboring ranches in cooperative practices like sharing labor and equipment to reduce costs and increase efficiency.

II. Social Capital Investment Firms

Bill Stoddart is a former fellow with the RSF Integrated Capital Institute, founder and president of NorthFork Financial, and co-founder of HomeStake Venture Partners in Bozeman, Montana. Stoddart talked about raising capital for sustainable agriculture. He focused on the ways in which private investors, nonprofits, foundations, and benefit corporations are offering a variety of models—mortgages to farmers, farm-friendly ground leases, lease-to-own arrangements, and low-interest revolving loan funds—to provide agricultural organizations access to land and operating capital. The limitation of this kind of capital is that these companies tend to work with sustainable farm and ranch operations, and in some cases, limit funding to organic producers. Social capital investment groups include RSF Finance, Iroquois Valley Farms, the Farmer Veteran Coalition, Neighborworks, FarmLink (depending upon the state), and HomeStake Venture Partners. "One of the key elements for getting impact investors on board is helping them realize that investing in farmland and farmers, especially those who are committed to rebuilding soil health, is not a high-return proposition, rather, it's a long-term commitment to establishing and maintaining food security," says Stoddart.

An example of a social capital investment firm that assists farmers and ranchers is Iroquois Valley Farmland REIT (Real Estate Investment Trust), a triple bottom line company providing opportunities for investors interested in social and environmental benefits along with financial gain.

Iroquois Valley Farms

Iroquois Valley Farms provides a uniquely corporate and indefinitely scalable equity investment opportunity for investors that want to make a difference while making a return on capital. The socially responsible Company follows triple bottom line principles looking for social, environmental, and financial returns. Using Rule 506(c) of Regulation D as regulated by the Securities and Exchange Commission, Iroquois Valley Farms raises money from individuals, family offices, foundations and other institutional investors that meet the definition of Accredited Investors (as defined by Rule 501(a) of the Securities Act).

Iroquois Valley offers affordable leases and mortgages to certified organic and transitioning farmers. Recently incorporated as a REIT, Iroquois Valley is committed to working with the next generation of organic and regenerative farmers to grow healthy food, restore soil, and regenerate ecosystems. The REIT has purchased or financed over 12,000 acres of farmland (including land later sold to tenant farmers) in 14 states, including Montana.

Farmer and innovator Anna Jones-Crabtree of Vilicus Farms in Havre, Montana, has been working with Iroquois Valley for several years. She and her husband were the first farmers in Montana to do so. “Unlike other farmland investment entities, Iroquois Valley’s first question wasn’t ‘what’s your return on investment,’” says Jones-Crabtree. “They wanted to know about us, our diversified organic production system and what we needed to make our business viable. They invest in the farmers first and foremost because they know farmers are the ones who are doing the hard work of building real equity in the soil."

Iroquois Valley offerings for farmers:

- Land purchases for active farmers
- Five-year leases, with automatic two-year renewal provisions
- Potential of a lifetime lease
- Rent based on the purchase price of the land
- Base rent with a variable rent payment when an operation reaches a certain level of profitability
- Mortgage funding: five-year fixed-rate terms with interest-only payments
- Refinancing to consolidate debt
- Farm equipment financing

Crowdfunding to raise donations and investments was discussed as one of the services social and capital investment groups can offer. Due to changes to the federal securities laws in 2015, producers can crowdfund directly through platforms like Kiva. Many states followed suit and now allow intrastate crowdfunding to raise money from a large group of nonaccredited investors. In Montana, state law allows it under the following circumstances:

- Company must be formed in and registered with Montana Secretary of State.

- Investors must be Montana residents.

- Nonaccredited investors can invest up to $10,000.

- Company may raise up to $1 million in any 12-month period.

- Costs include filing fees and preparing stock, disclosure, and subscription documents.

Sample Deal

Lease agreement: 54% of revenue to farmer, 46% to the value-added corporation, plus a say in the crop mix.

Exclusive sales agreement?

Corporation pays 50% of a subset of production costs, including: labor, fuel, seed, repairs, and maintenance.

Exit strategy: Terminable at will, a few months notice required.

Recent investments are mostly for young farmers expanding their operations, whether they be specialty grains, pastured dairy or livestock. In 2016, they purchased 320 acres and later purchased another 960 acres in transition in Montana and leased it to Vilicus Farms to help them expand their certified organic dryland farming operation outside of Havre. Over 70% of the farms leased by Iroquois Valley Farms are to millennial tenants, utilizing the company's Young Farmer Land Access Program. Consequently, the company and its member investors are well positioned to benefit from the growth of local and organic foods produced by an expanding base of mostly young farmers.

By supporting a range of educational, local foods and sustainable agriculture initiatives, the company has developed a broad pipeline of prospective tenants and is continuously financing farmland for these regenerative organic family farmers. While past performance is no guarantee of future results, long term investors have been consistently rewarded with the growth of their capital. Iroquois Valley is actively seeking young farmers with a diversity of farming operations, including grains, local and organic foods, vegetables and pastured livestock. If you are a young farmer interested in growing your sustainable agriculture farmland acres, get in contact.

Model: Purchase farmland on farmer's behalf and lease back to farmer.

Lease Terms: 5 year initial term, with 2 year renewable evergreen thereafter unless cancelled by either party.

Lease Structure: Variable cash rent, payable semi-annually

Base Rent: Calculated to return a 3.5% ROI on entire acquisition costs of acreage, plus actual real estate taxes and annual property, casualty, and liability insurance premiums.

Variable Rent: One third total revenues over variable rent threshold; where threshold is calculated as 3 times the base rent (excluding real estate taxes and insurance premiums) in each year. All revenues calculated using non-GMO conventional or contracted organic transitional crop prices and actual production until organic certification is obtained, with organic crop prices used thereafter.

Maximum Rent: At no time will the base rent, excluding real estate taxes and insurance premiums, plus variable rent due exceed 10% of all in acquisition cost of the leased farmland property.

Maximum Purchase: _____ per survey acre or $_________ for all acreage, excluding closing costs.

Homestake Ventures

Investor money into coops. Fixed income portfolio, diversified real estate portfolio. Farmland LP in Northern California--model is unclear, need to find out more about their exit strategy. Expected margins unrealistic. Boston Impact Initiative, Deb Freeze, combo of family and community foundation investments applied to inner city environment.

They just closed their first deal on farmland. Market rate loan in partnership w FSA, bank and private equity partners the farmers brought in. Structured around revenues with seasonal sensitivity for payments. Part of Integrated Capital Fellowship, a national group to find solutions to major issues like enviro damage, social inequity, etc. Combining human, natural and financial elements with grants, donations, concessionary, PRIs, MRIs, standard debt, etc. RSF Social Finance is the lead on this project. Bill started figuring out how to help local community members invest in local projects. Complicated. Started CEED net to try to raise $2 million for a fund. Too many limitations in the model. Partnered with Jeff to form Homestake Project: a network of subscribers, mostly Bozeman at this point but want to be statewide. They pay a subscriber fee for the partners to research and find deals. They test the waters around a deal. Once enough people subscribe, they ask the company to help with closing costs and go on to due diligence. Community building exercise. They don't have a committed fund, but then Homestake has to sell the deal to the investors.

1. Different levels of subscriptions--most expensive puts you first in line on a deal. If a $500k deal and you subscribe $100k, you and four others can take on the whole deal. If there is any money left, it goes to the next level of subscribers.

2. Deals range from start up capital to fully collateralized debt. Looks for businesses looking to grow or transition (family farm works here). Valuable community partner businesses that they don't want to see go out of business.

3. Exit strategy--no exit as to the business itself. Target internal rate of return--paid back over a 10 year period at a 10% return. Once the IRR is hit, they the investor is paid back and everything else is profit.

III. Community Land Trusts

Given farmers' and ranchers' strong ties to the land, and the underlying Montana ethos of private property rights, we were surprised that people were so open to the idea of putting the land into a community land trust to ensure it remains affordable and in production for the future. The idea of owning the improvements on the land, not the land itself, sat comfortably with a number of farmers as long as they had land security in the form of the 75-year renewable, inheritable, transferable ground lease. Trust Montana's and Agrarian Trust's presentations on this model generated great enthusiasm at the summit.

Agrarian Trust is a national organization that formed in 2013 to protect farmland for sustainable agriculture and preserve affordability for new and disadvantaged farmers. The model utilizes the community land trust concept, where the nonprofit organization owns farmland in order to provide permanent affordability and ensure the land stays in agriculture. Agrarian Trust operates on a national level. Applying a "commons-based" approach, it helps landowners and retiring farmers partner with beginning and under-resourced farmers by making sure the retiring farmers receive a fair price for their land, while offering long-term leases to the beginners who can't afford the high cost of entry into the agricultural economy. Through lease restrictions and agricultural easements on the land it owns, Agrarian Trust can remove barriers to owning land require organic farming practices, maintain affordability for future farmers, and ensure that sensitive ecosystems are protected. Agrarian Trust raises capital to purchase some land, but the most common method of acquiring land is through donations. As the organization continues to develop, Agrarian Trust will transfer donated land to its 501(c)(2) title-holding corporation or to partner organizations operating at the local level.

Agrarian Trust

At the summit, Ian McSweeney, Agrarian Trust's executive director, expressed interest in partnering with organizations and farmers in Montana. Agrarian Trust has the potential to help with raising capital and providing some technical assistance. Local nonprofits with state-specific knowledge and legal expertise, such as Trust Montana, could hold the land in trust and oversee the day-to-day permanent affordability restrictions—vetting buyers at resale, monitoring land use restrictions, and enforcing farming requirements and resale formulas.

Trust Montana Director Hermina Harold says CLTs are a flexible tool that can help both rural and urban areas in need of affordable farmland, housing, and commercial space. Trust Montana's approach is to serve the whole state with one central CLT in order to increase the livability of communities for all Montanans. Because CLTs have to build up a large portfolio in order to become self-sustaining, most rural areas would not be able to utilize the CLT tool without a larger entity like Trust Montana.

IV. Stacking Tools

Stacking multiple tools to increase affordability of, and access to, land is not technically a new tool, but it's an approach that many summit attendees found inspiring. Ranchers like Bart and Wendy Morris of Oxbow Cattle Company have used conservation easements, agency funding from federal farm programs, CSAs, grass banking, and creative partnerships with nonprofit groups to start and grow their operation.

It's important to note that traditional farm financing still plays an important role in funding agriculture in this country. One of the main functions of the creative finance tools at this point is to provide a bridge for beginning farmers and ranchers to help them develop the business plans and gain the experience that traditional farm finance companies like the Farm Service Agency and Northwest Farm Credit Services require in order to qualify for their programs. Loans from FSA and other traditional ag lenders are an important stacking tool.

Next Steps

Having accomplished our short-term goals, the summit organizers—the Community Food and Agriculture Coalition of Missoula County and Trust Montana—are now forming committees and working with the relevant experts on next steps. Over the next two years, the two organizations and pilot project partners will develop the identified tools so they may be marketed statewide and utilized to fulfill the overarching goal: more Montana farmers with secure land tenure and viable farm businesses.