

# Conserving Farm Real Estate Value

Value is defined as a fair return or equivalent in goods, services, or money for something exchanged; marketable price; relative worth, utility, or importance; or degree of excellence. The goal of most farm businesses and farm families is to build wealth and earn a living so the family can increase its quality of life. Prudent action and management to preserve the value of owned farmland is part of the long-term, wealth-building goal.

Farm real estate constitutes the overwhelming bulk of assets owned and managed by farm operators. In 1992, the United States Department of Agriculture reported farm real estate in the United States had an aggregate value of \$633.1 billion and total assets used in the farm sector were \$861.5 billion. Real estate represents more than 73 percent of the assets owned and managed by U.S. farm operators.

In Kansas, farm real estate was valued at \$21.6 billion in 1992, and total assets managed by farm operators were \$30.7 billion. Farm real estate comprised 70.4 percent of total assets in Kansas.

Only about 3.5 percent of farmland changes hands each year, but, despite this low turnover rate, the amount and value of land transferred each year is substantial. Sale contracts between unrelated individuals accounted for half of the 29 million acres, valued at \$21 billion, transferred in the U.S. in 1988. About 18 percent was transferred through sales between relatives. The remaining 31 percent of farmland was transferred as a result of inheritance, gift, or other nonmonetary contractual terms. With half of farm real estate transfers between family members, strategies to conserve real estate value provide benefits to the current and future family farm owners.

Many farm families view their real estate holdings as both investments and part of their family heritage. Both views provide a motive for conservation of farmland value. Farming activity provides income for farm families as well as a home for the current and future generations. Conserving the value and quality of farmland, the improvements used in the farm business, and the family home secures a better financial and family future. Family members have daily and continuous contact with their home environment. Farm workers have seasonal or daily contact in the working farmstead area, livestock facilities, and the cropland area

of the farm. Guests at the farm also have exposure to the farmland and farmstead environment. All deserve the highest possible quality of environment in which to live, work, and visit. Detriments to this environment may be perceived as hazardous to the marketability and value of the real property.

This fact sheet is designed to motivate farmland owners to consider the impact of their actions on land value and to choose actions in their self-interest. Conflicts between public and private interests will persist, however, there are many instances in which action in self-interest will serve the public interest.

## Issues and Factors Affecting Real Estate Value

Academic and appraisal studies have identified numerous factors that contribute to the value of farm real estate. Like money, real estate has value in use and value in exchange. Farmland is both a factor of agricultural production and an investment. Some of the factors contributing to the value of real estate are outside the control of the owners. Other factors are directly influenced by the management decisions of the owners and tenant operators.

Economic and social forces that influence the farmland market are outside the owner's control. Fundamental changes in production technology or systems of technology may render current systems obsolete, thus reducing their marketability and value. Fiscal and monetary policy influence the general economy and can have direct effect on the value of real estate, especially through the interest-rate mechanism.

Changes in government policy also influence value, either by changing the income-producing potential of property or by changing the public services available to support or protect an owner's investment. Local tax rates, environmental regulations, zoning, building or health codes, and public access to privately owned property are often restrictive influences on value beyond individual control.

Natural forces of climate, topography, inherent soil productivity, and the availability of water resources for domestic or agricultural use are also basic to property value, but not controlled by the property owner. The location of a property in relation to population centers, transportation systems, and mar-

kets for agricultural production is viewed as a major factor of value. While location is static, there may be changes in population, transportation, or markets that affect value.

Inherent to farm real estate value is its use value. Property has utility if it satisfies human wants, needs, or desires. Because people have differing utility, or degrees of wants, needs, and desires, they often do not have the same concept of value. The market value of farming may be different from the market value of recreation. An owner may receive benefits from farming activities, recreational activities, and other uses of the real estate as long as there are no legal restrictions on the property rights. Society may see value in a property due to its historical significance.

Other factors of value may be under the control of the owner and operator. When someone offers a tract of real estate on the market, they offer certain rights for the use of that real estate. This “bundle of rights” includes the interests, benefits, and rights inherent in ownership. Prior agreements may have transferred some of these rights to others, such as mineral interests, easements for public roads, or life estates allowing someone the full use of the property for their lifetime. Actions of owners can impact the bundle of rights that can be offered to the market and thus affect the marketability and value of the property. Decisions regarding ownership, the titling of land to multiple owners, and leasing to third parties may become detriments to value if they reduce the future rights to the use of the land. Owners may cause questions of ownership to arise in the future if they allow title blemishes to occur or remain unquestioned. Maintaining a clearly defined title to real estate can contribute to its marketability and its market value.

The presence and condition of improvements have a direct influence on the market value of real estate. The owner who maintains the condition of improvements has control of this dimension of value. Conserving total value means protecting the land itself and its improvements from anything that decreases market value.

Environmental hazards can have a direct effect upon the salability and the mortgagability of farmland. Hazards that threaten the health and safety of landowners and farm operators or their employees and families may decrease the market value of farmland and improvements. The salability of a farm depends increasingly on a formal or informal environmental assessment of the property. Potential buyers are advised to be fully informed about the attributes of a tract. A chain of responsibility and liability for environmental hazards on farmland involve past, present,

and future owners. Since the mortgagability of land depends upon its salability, environmental hazards may drastically reduce the net recovery value of property and limit the extent to which the property can be used as security for credit. This may limit the mortgagability of the tract for a prospective owner's purchase financing. It also may limit the credit available to the current owner for improvements to the real estate or for other investments financed by a mortgage on current holdings. Prudent buyers of farmland will become fully informed about the prospective purchase. Buyers will likely give higher bids on properties that are free of environmental hazards.

Water is a precious resource for life and farming. Water issues involve the water supply system available on the real estate, the status of permitted water use, and the quality of groundwater and surface water resources affected by the use of the property.

The landowner should protect any domestic, livestock, and irrigation water sources from contamination. Water well location is a controllable factor for the owner. The condition of the wellhead area can have an effect on water quality and the potential for future groundwater contamination. Abandoned wells should be plugged or managed according to the requirements of appropriate authorities. Water should be tested to determine if it is adversely affected by management decisions and to ascertain if it is suitable for its intended use.

The right to use allocated water resources should be maintained to enhance real estate values. Required permits, records of use, and reports will support the future water right claims of current and subsequent owners. Irrigation systems that utilize fertigation and chemigation technology should have the required safety equipment and be managed and maintained to reduce the risk of groundwater or wellhead contamination.

Domestic and livestock waste systems are attributes of a farm tract that affect marketability. The age, size, and location of domestic waste systems are important considerations for owners, potential investors and mortgagees of developed farmland. Permitted systems that are maintained adequately and meet inspection requirements support or enhance marketability and value. Outdated systems or those that have been poorly maintained may be detriments to value.

Livestock waste systems, including storage and disposal areas, have a direct effect on the use value and market value of farm property. Systems must meet the requirements of the law, increasingly affecting nearly all types and sizes of confined livestock systems. A poorly managed system may contribute to soil and

water contamination to an uncertain degree, however the marketplace often discounts values in the face of uncertainty. Correction of severe problems may be technically difficult and expensive.

Solid waste collection and disposal services in rural areas are improving. However, practices followed by prior owners may be a detriment to land value. Abandoned dumps are potential hazards to both the environment and land value and should be properly cleaned up to reduce the risk of further water and soil contamination. Unsightly refuse areas will likely be a detriment to the marketability and value of property. Likewise, the disposal of animal carcasses should meet the requirements of the law to minimize current and future liability for damages.

Should there be hazardous waste contamination of soils, the costs for the clean-up, removal, and safe storage of these materials may be significant. Owners should be highly motivated to know and follow recommended practices for handling wastes that are potentially hazardous.

Liquid-material handling on farms presents special challenges for the landowner. Fuel and chemical storage and handling are recognized as potential hazards to surface and groundwater sources and soils. Fuel storage and fueling areas should be sited away from water sources. Underground storage tanks should be monitored or removed before leaks can occur. For large aboveground storage facilities, properly designed and maintained containment structures will reduce the risks of major spill damage.

Pesticide training includes emphasis on safe storage, mixing, application, and rinsate disposal for all farm-use pesticides. Safety practices focus on health and environmental issues that also protect real estate values from the adverse affects of a chemical spill or contamination. Pesticide storage areas should be located away from other farm improvements and properly identified for safety, fire, and health agency personnel.

Landowners and farm operators should have contingency plans to follow in the event of an accidental spill, a fuel or chemical leakage, or a natural event that contributes to the potential for an environmental hazard on their property. Such a plan can minimize the damages and help control the costs of remedying any problem.

Mineral and mining activity on farm real estate can affect value both positively and negatively. Where the mineral rights are no longer connected to the surface rights, mining or oil extraction activity may be a detriment to value, particularly if surface restoration is not required of the mineral operator. Landowners

contracting with mineral exploration and extraction companies should protect their surface rights and ensure they are compensated for any hazards to current or future value.

Building characteristics may affect value in both positive or negative ways. Structures with hazardous materials, such as asbestos, lead plumbing systems, or lead-based paint, may be detriments to value. Removal and disposal of these materials may be difficult and expensive. Disposal of storm-damaged buildings that contain hazardous materials may present special challenges for landowners.

Landowners may overlook potential positive attributes of value stemming from historic buildings or sites on their properties. Homes, barns, and other improvements may have significant historic and potential tourism value. Knowing the pre-settlement and post-settlement history of your area and the history of your own property ownership may pay economic dividends and enhance personal enjoyment from ownership.

Natural features of real estate may also be unique to an area or genuinely rare in nature, suggesting the potential for future market exploitation. Unique wildlife habitat may be an attribute of the land worth preserving for future enjoyment.

Conservation Reserve Program leases protected many acres from erosion hazards in return for annual payments. Long-term conservation plans preserve farm eligibility for deficiency payments and crop loan options. Following the provision of these contracts preserves the potential for financial rewards for the current, future and, in some cases, prior owners. Breaching these contracts will almost always have a negative effect on farmland value. Conversion of farmland to nonfarm use may have market values that justify a decision to terminate a CRP contract during its term. These and other contractual agreements can affect market values.

Easements and rights-of-way are other contracts that affect farm value. Owners may grant easements to public and private entities in return for some fixed single or annual payment. In the case of mineral activity, it is advisable for the owner to negotiate a fair settlement and to ensure there is compensation for any future damage to property as a result of the easement. Provisions of wetlands easements include compensation for the landowner, however owners should recognize there will be limitations on the private use of this land in the future for perpetuity. This may affect the future marketability and value of the property as well.

The environmental liability of farmland ownership extends literally downstream and into the future. Causing damage to surface or groundwater may be a violation of state or federal law and result in a fine or civil lawsuit or both. Defense against such claims is expensive and uncertain, even if such claims are unfounded. Farm owners, managers, and operators who reduce the likelihood of environmental damage are acting in self-interest to reduce future costs and to conserve real estate value.

## Implications

Value of farmland has a broad definition and is affected by a variety of factors, only some of which are under the owner's control. Landowners and operators should be motivated to ensure the future value of the land resource reaches its ultimate market potential, undiminished by hazards. Stewardship of the soil and water resources found on farmland has an economic reward.

Legal decisions of landowners also affect value. A property with a clear title of ownership has greater market value or lower costs of transfer than a property with a blemish on the title. A property with no easements, or properly drawn easements that protect the remaining rights and privileges of the current or future owners, has more value than a property burdened by badly drafted easements. Properties with significant historic structures or unique natural or wildlife resources have enhanced potential future value.

Conserving farm real estate value is in the long-term best interest of the landowner. Managing to eliminate liabilities for environmental damages in the present and future and the accompanying legal costs and penalties protects the income potential, future marketability, and market value of farm real estate.

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