Farm Tenants: Be Cautious with Permanent Improvements to Leased Land

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Farm tenants may identify how rented land could be made more productive (e.g., by installing drainage tile or applying lime), or how the farming operation could be made more efficient (e.g., by constructing on-farm grain storage). Such improvements often increase the value of the land, or at a minimum have multi-year benefits, and are typically the responsibility of the landowner.

What if the landowner declines to make the improvement? Should the tenant consider making the improvement at tenant’s expense if the landowner is agreeable? As a general rule, farm tenants should make such improvements only with great caution.

The problem. Most Illinois farm leases are year-to-year leases or, if for a specific term, rarely for more than a one-year term. The desired improvement, however, may add permanent value to the property or at least create benefits that span many years. If the tenant has no enforceable guarantee that the tenant will keep the farm for many years, the tenant runs the risk of being asked to leave the farm before the useful life of the tenant-financed improvement has ended. Thus, the landowner and the new tenant might receive a substantial windfall (the continuing value of the improvement) at the expense of the previous tenant (the one who made and financed the improvement).

Can the outgoing tenant remove the improvement when leaving the farm? Theoretically, at the end of the lease term a tenant can remove certain improvements (i.e., “removable fixtures” added by the tenant) in some circumstances. In contrast, Illinois law provides that permanent improvements usually may not be removed by the outgoing tenant. Legalities aside, improvements such as drainage tile or on-farm grain storage made by the tenant at tenant’s expense, or agricultural lime applied by the tenant at tenant’s expense, are not very removable as a practical matter.

Is the outgoing tenant entitled to compensation for the remaining value of the improvements made at tenant’s expense? Absent special agreement, the right of an outgoing tenant to be reimbursed for these improvements is questionable. However, if the tenant and landowner have a binding agreement regarding the tenant’s right to be reimbursed, the tenant is entitled to compensation as provided in that agreement. Therefore, as a general rule, a farm tenant should not make such improvements to rented land unless the tenant has an enforceable agreement containing acceptable reimbursement terms if the tenant leaves the farm.
In summary, farm tenants should be very cautious when making or paying for permanent or multi-year improvements to rented farmland. Legal counsel can help the tenant understand the legal implications and financial risks accompanying such expenditures. If the tenant still wants to proceed, legal counsel can advise the tenant regarding suitable lease provisions or separate agreements that would obligate the owner to compensate the tenant fairly if the tenant leaves the farm before the improvements made by the tenant have been fully depreciated.

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