Restriction of Farm Ownership as Rent-seeking Behavior:

Family Farmers Have It Their Way

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ABSTRACT. Restriction of *foreign ownership* of *U.S. farmland* has an obvious cost of foregone *capital gains* to *farmers.* Yet their push to achieve state *regulation* of *foreign investment* in *agricultural land* has a sound *economic* basis. If required acreage expansion and high prices for land combine to force *small, family farmers* out of business, the value of their accumulated *human capital* falls precipitously, since it is soil-specific. With a large foreign demand for farmland which induces a tremendous rate of *land-price inflation,* capital gains on their land swamp potential human capital losses. However, marginal participation in the U.S. farmland market by foreigners creates capital gains on land which are insufficient to compensate farmers for lost human capital, and creates a rationale for regulation. The empirical results demonstrate that the pattern of *legislative restrictions* against foreign ownership of farmland is a function of the relative *political power* wielded by family farmers.

I

Introduction

IN THE DECADE of the 1970s, foreign direct investment in America, particularly in U.S. farmland, has been the focus of a great deal of attention, inspection, indignation, and, ultimately, regulation. To an economist such indignation and regulation appears at first, and even second, glance to be "irrational." An efficient economic order requires that resources be allocated to their most highly-valued uses regardless of the final distribution of property rights. Yet the facts remain: along with the spate of purchases of U.S. real estate by foreigners in the 1970s has appeared a growing avalanche of state and national regulation. Where regulation had not appeared as of mid-1981, it was not due to lack of effort in the state legislatures.[1]

In this paper a plausible explanation for the emergent pattern of restrictive legislation is presented and analyzed in terms of several persistently unanswered questions *vis-á-vis* foreign investment in America. It is argued that owners of small, family farms are net demanders of U.S. farmland, and are consequently

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desirous of low prices of land. In typically rational economic fashion, they will attempt to depress land prices via the political process (among several alternatives) so long as the marginal benefits, in terms of lower prices, outweigh the marginal costs of doing so.

In the following section, a model which stresses the demand for protective legislation by small, family farmers is presented as a plausible reaction to the presence of foreign buyers in the domestic land market. A brief introduction to the phenomenon in question provides the setting for that model. Empirical testing of the model with respect to the pattern of nonresident alien land ownership restriction is provided in Section III, utilizing information provided by the various states, and farm population statistics. Concluding comments are offered in Section IV.

Table 1

Major State Restrictions of Foreign Ownership of Farmland

	State	Restriction
1.	Arkansas	NRA ownership not allowed
2.	Connecticut	NRA ownership not allowed
3.	Illinois	NRA must dispose of holdings within 6 years
4.	Indiana	320 acre limit vis. NRA's
5.	Iowa	NRA ownership not allowed
6.	Kentucky	NRA must dispose of holdings within 8 years
7.	Minnesota	NRA ownership not allowed
8.	Mississippi	NRA ownership not allowed
9.	Missouri	5 acre limit vis. NRA's
10.	Nebraska	NRA ownership not allowed
11.	N. Dakota	NRA ownership not allowed
12.	Oklahoma	NRA ownership not allowed
13.	Pennsylvania	5000 acre limit vis. NRA's
14.	S. Dakota	160 acre limit vis. NRA's
15.	Wisconsin	540 acre limit vis. NRA's

Source - Monitoring Foreign Ownership of U.S. Real Estate, Vol. 1, U.S.D.A. 1979, pp 61-92

II

Restriction of Foreign Ownership of Farmland: The Politics of Redistribution

As of mid-1979, 15 states had placed major acreage or other restrictions on nonresident alien (NRA) ownership of farmland, and the legislatures in several additional states had considered or were considering passage of similar restrictions. (See Table 1).

An economist evaluating the problem from an efficiency viewpoint would conclude that there should be no restrictions on foreign ownership of U.S. farmland (or any other kind of land), and that farmers have nothing to complain about. As Public Choice theorists have demonstrated repeatedly in recent years, however, much real world behavior is related to attempts at influencing the

distribution, as opposed to the size, of the economic pie. Individuals or groups will attempt to influence terms of trade (via threat postures, information gathering or distortion, and the political process, to name only three means) up to the point where the discounted marginal expected benefit of seeking influence is equal to the marginal cost of engaging in such activity.

It is well known that agricultural interests maintain extremely effective lobbying organizations. Farm organizations are the only identifiable interest groups pushing legislation which restricts foreign ownership of U.S. land. A theory which purports to explain the pattern of such restrictive legislation is faced with the task of providing reasonable answers for the following questions:

(1) Why do restrictions emerge from an incidence of foreign participation in the domestic land market which is minuscule?

(2) Why are restrictions imposed upon nonresident aliens only?

(3) Why are restrictions targeted specifically for domestic farmland rather than other real estate investments by foreigners?

The basic issue raised by question (1) above concerns the "rationality" of farmers when they try to depress the demand side of the market for agricultural land. The rationale for regulation is not obvious, and requires more than a cursory look at the occupation of farming. Not only is the foreign presence in the domestic land market exceedingly small; any restriction of the demand side of the market causes losses (on paper) in the rate of capital gains appreciation in the value of the land currently held by farmers (the internal margin).

Farmers as a whole can be classified as either (1) owners or tenants of large farmland holdings and (2) owners or renters of small farms. Farmers who fall into the second category, the so-called 'family farmers,' seek gradually to expand the acreage they own by purchasing or renting acreage near or adjoining their farms, since acreage which is spread hither and yon becomes costly to operate.[2] The motivation for this demand for additional farmland apparently stems from the steadily increasing size of the minimum-acreage farm consonant with capture of all relevant scale economies.

The available statistics tend to bear out the validity of this setting. By far and away the large majority of farmland transfers which take place each year occur between farmers. In 1976, for example, 65 per cent of the land transferred went to active farmers.[3] In that same year, farm enlargement accounted for 63 per cent of all farm tract purchases.[4] This dual trend of declining absolute numbers of farms and increasing average acreage per farm is chronicled in Table 2.

In order to comprehend why it is rational for farmers to push restrictive legislation, one must first understand the manner in which they are affected by the trends exposed in Table 2. In the absence of any speculative motive,

maximization of the present value of holdings—the rationality precept embraced by virtually all professional economists—precludes attempts by farmers to restrict the demand side of the market; competition among suppliers precludes restriction of the supply side. However, when consideration is given to farmland in its capacity as a factor input into the farmer's production process, the conditions emerge which must exist in order for farmer-supported restrictions on NRA ownership of farmland to be consistent with assumed rationality. It is clear that two conditions must be satisfied:

(1) Farmers must be net demanders of farmland, and

(2) marginal benefits accrued as a result of restrictions must outweigh marginal costs of achieving regulation.

That segment of the farm population which is comprised of active or potential

Table 2

Number of Farms and Average Farm Size

Year	Number of Farms (1000)	Average Acreage per Farm
1979	2,330	450
1975	2,491	427
1964	3,158	352

Source: Statistical Abstract of the United States. 100th Ed., 1979

sellers of land will naturally prefer unrestricted demand in order to maximize land price inflation as a means of reaping capital gains on the value of their landholdings. In this instance, the factor of production aspect of their land serves as a non-binding constraint of the behavior of farmers.

When farmers are net demanders of farmland, either for speculative or productive purposes, they have a legitimate interest in attempting to manipulate the market in order to obtain farmland at prices which are relatively favorable. Demand for additional land by family farmers occurs for two reasons: (1) as a response to knowledge or expectations regarding the structure of their chosen occupation over the course of their life-cycle, and (2) in response to exogenous shocks in technology. As a result, net demanders of agricultural land may not act so as to maximize the present value of their holdings at all times. This result is predicated upon the costs associated with inter- and intra-occupational mobility with respect to farmers.

It turns out that 82 per cent of farmers in 1962 had fathers who were farmers.[5] This high degree of occupational inheritance is explained by Laband and Lentz (1983a, b) in terms of the comparative advantage obtained by farm youngsters

in the occupation of farming, relative to otherwise-identical, nonfarm youths, as a byproduct of growing up on a farm. In the family production process which characterizes farming, a son assists his father with the farm operations. He acquires, through experience and through his sire, information about the farm for free, which would otherwise be very costly to obtain. Relative to otherwise-identical, nonfarm youths, he has lower costs of entry into farming as an occupation. However, sons who choose to work the family farm have farm-specific skills which would not be very valuable in the event required expansion and the high cost of farmland combined to force them out of business, and into the job market.

A rise in the value of agricultural land may adversely affect the value of farmers' human capital in the following manner. Assume the typical farmer owns a quantity of land which enables him to barely capture all relevant economies of scale in production. As advances in technology push the minimum acreage requirement higher, the farmer is forced either to expand his operation, or else sell his operation and become a tenant farmer or a farm manager, or enter a completely different occupation. In any capacity other than as owner-farmer, the value of this farm-specific human capital is lower than when he is the owner; while at the same time he foregoes capital gains on the value of the farmland.

Insofar as the vast majority of farmers resemble, situationally, the 'typical' farmer portrayed above, and insofar, furthermore, as a high percentage of them opt to expand their holdings of land, restriction of the demand side of the market for farmland would be in their economic interest, providing the marginal gains, in terms of lower purchase prices for land, outweigh the marginal costs of obtaining regulation.

In this model, farmers are represented as maximizing the net value of their capital at all points in time. There are two components of this capital:

(1) the farmland itself, and

(2) the human capital associated with utilizing the land in its capacity as a factor of production.

The basic point to be gleaned from the discussion above is that incremental increases in the value of land may adversely affect the value of farmers' human capital. But, a large foreign presence in the U.S. land market—one that contributes significantly to a tremendous rate of land price inflation—will be largely ignored by farmers. Gains on the capital value of their physical assets would swamp the damage done to their human capital, and farmers could go to the beach and live off of their net capital gains.

With respect to farming as an occupation, maximization of net capital corresponds to maximization of lifetime net wealth. This assumption regarding

farmer behavior provides simultaneously a rationale for the push for restrictive legislation against foreigners while satisfying the economists' precept of rational behavior on the part of farmers.

Note that small changes in land prices are not sufficient to permit the capital gains to overwhelm the loss in human capital value. Below a certain threshold, such changes may do more damage than good as far as small, family farmers are concerned, and regulation emerges as a vehicle to restore the rate of land-price increase to its optimal value, in terms of maximizing family farmers' net wealth. The answer to question (1), posed earlier, is: regulation of foreigners occurs precisely because incidence of participation by them in the market for farmland is small.

It would probably be too costly for farmers to restrict other Americans or resident aliens from buying farmland, even though they might wish to do so in an effort to restrict demand, keeping prices low. The cost of legislating against foreigners is undoubtedly much lower. Net benefits to family farmers in terms of lower land prices or reduced rates of farmland price increase may outweigh the costs associated with lobbying for protective legislation, *on the margin.* This provides an answer for the second question posed earlier—NRAs are targets of regulation because the cost of discriminating against them is relatively low. It just doesn't cost very much to buy votes against foreigners, either directly, or indirectly, by putting the fear of foreigners into the minds of the voting public.

Regulation emerges, then, out of a struggle between those large farmers who are potentially net suppliers of farmland, and small, family farmers who are net demanders of farmland, for the infra-marginal rents associated with land-price changes which result from foreign participation in the market for U.S. farmland.[6] We can now suggest an answer to the last of the three questions posed earlier, namely, why are restrictions targeted specifically at domestic farmland rather than all real estate investment undertaken by foreigners? In this model, the principal interest groups are concerned only with farmland, to the exclusion of other types of foreign investment. It is strictly a distributional struggle between farmers, which happens to involve also a couple of other groups as interested parties.

In summary, this rent-seeking model of legislative restriction of farmland ownership by foreigners is based upon the dichotomization of farmers into a class of large landowners who are net sellers of land, and a class of small, family farmers who are net demanders of farmland. Members of the latter group will seek to inhibit the demand for farmland in their respective states whenever the expected marginal benefits of such efforts exceed the costs. This implies

that the pattern of restrictive state legislation can be explained in terms of the relative political power of family farmers on the one hand, and farmers with large landholdings and realtors (the other principal opponent of restrictions) on the other. This implication is tested in the following section.

III

The Politics of Redistribution: Testing the Model

TWO CLASSES OF FACTORS are involved in attempting to predict whether or not the family farmers in any specific state will be successful in their effort to restrict foreign ownership of farmland:

(1) the political clout enjoyed by family farmers relative to that wielded by large farmers and realtors, and

(2) the absolute amount of political power obtainable by family farmers, which is governed by institutional and demographic factors.

The latter class is explored by McCormick and Tollison.[7] They argue that the success of influence-buying in state legislatures is affected by a number of factors, including the size of the legislature, the ratio of the sizes of the two chambers in bicameral legislatures, and the size and per capita income of the state's population. Agricultural interests must be well-represented in the state legislature, either because the number of farmers relative to the entire state population is large—the vote-*counting* theory of influence, or else because agriculture represents a substantial portion of the state's income—the vote-*buying* theory of influence, as amended by McCormick and Tollison. It should not necessarily be the case however, that a preponderance of agriculture in a state, however measured, will ensure restrictions on foreign ownership of land, since those agricultural interests must then overcome opposition in the legislature.

All other things being equal, one should witness an inverse relationship between the success of family farmers in obtaining regulation and the political clout wielded by opposition groups. The opposition is headed by individual farmers with large holdings of land, the National Association of Realtors, and occasionally by a state Chamber of Commerce.[8] States in which the Association of Realtors is large are, in fact, virtually free of farmland regulation, especially throughout the sunbelt, where recent population in-migration has incited a boom in the real estate industry, and a consequent strengthening of the political power enjoyed by the states' realtor associations.

The rent-seeking model of restrictive legislation implies that the observed pattern of regulation can be explained—at least in substantial part—by the political strength of the two opposing factions relative to each other, and by

the relative importance of agriculture to the state in question. This dependency is modelled in Equation [1] and explained below.

$$REG = a_0 + a_1YPC + a_2POP + a_3RGNP + a_4RFR + a_5FL + u, \qquad [1]$$

where REG = a 0–1 variable which indicates the presence (1) or absence (0) of a "major" restriction against NRAs[9],
YPC = per capita state income,
POP = state population
RGNP = the ratio of agricultural product per capita to per capita Gross National Product,
RFR = the number of farmers divided by the number of realtors in that state,
FL = the proportion of the state legislature composed of farmers,
u = a random disturbance term.

One measure of the costs associated with achieving regulation is the percentage of seats in the legislature which are held by farmers (FL). The presumption is that a farmer/legislator can marshall support for or opposition to a farmland regulation bill at much lower cost than can an ordinary farmer. For one thing, he obtains one legislative vote for free—his own. Second, he can engage in logrolling with other politicians as a means of obtaining additional votes, a method which is unavailable to farmers or realtors who are not also legislators. Before this variable can be signed there must be some presumption as to whether family farmers or larger farmers are most likely to be legislators. If legislatures are dominated by family farmers *qua* legislators, FL should be signed positive, and vice-versa if large farmers make up the bulk of the farmer/legislator crowd. Since it is unclear *a priori* which of these effects dominates, the variable will remain unsigned.

A second measure of the relative importance of agriculture to the state in question, an indirect predictor of farmers' influence in the state capitol, is the percentage of state income which is generated by the farming sector (RGNP). Since the greater percentage of output is produced on small, family farms, it is predicted that this variable will be positively related to the incidence of restrictive legislation *vis-à-vis* foreign ownership of farmland.

As argued by McCormick and Tollison, the wealth of a state's population (as proxied by income per capita YPC) influences lobbying in two ways. "As wealth increases, the costs to individual voters of monitoring the political process increase (a substitution effect), and the income obtained by a lobbying group should thus rise in wealthier jurisdictions. However, if monitoring the political process is an income-elastic consumption good, an argument that is often made, there is an income effect that cuts in the opposite direction from the substitution

effect.[10] They predict the substitution effect to dominate, and their wealth variable signs out correctly, if insignificantly. This provides some reason to expect YPC to be positively related to REG.

McCormick and Tollison also argue that more wealth transfers of the type discussed in this paper will be forthcoming in large populations than in small ones, as a result of free riding and shirking. In their words, "As population increases, the probability of any one voter's influencing collective decisions decreases. Moreover, for a given transfer, the per capita share of the costs falls

Table 3

Logit Regression Results for Major Restrictions (1976)

Explanatory Variable	Coefficient/Chi-Square	
Constant	-16.978795[b]	-15.588080[b]
	(5.26)	(5.44)
RFR	0.276664[b]	0.291910[b]
	(4.01)	(4.51)
YPC	0.001469[a]	0.001377[a]
	(3.09)	(3.17)
FL	0.385407[b]	0.397652[b]
	(4.26)	(4.84)
POP	0.000040[b]	0.000035[b]
	(4.26)	(3.91)
RGNP	10.253244	
	(1.49)	
Predictive Accuracy Coefficient	0.604	0.588
Correct	88.0%	86.0%

a - Significant at 0.10 level
b - Significant at 0.05 level

as P (population) increases."[11] It is expected that POP will thus sign out positive.

One measure of the comparative political clout wielded by the opposing groups is provided by a simple head count, by state, of the numbers of realtors and farmers (assumed to be dominated by the 95 per cent who are family farmers). It is predicted that the ratio of farmers to realtors will be related positively to presence of legal restrictions on foreign ownership of domestic farmland, i.e., RFR > 0. The more that farmers outnumber, and hence can outvote realtors, the greater the likelihood that the farmers' quest for protective legislation will not be thwarted by realtors.

Two versions of the model presented in Equation [1] were estimated using the logit procedure for ordinary least squares, where the dependent variable is dichotomous. The results of the estimation procedure are reported in Table 3.

The estimates strongly support the contention that the presence of restrictive legislation is positively related to the political power wielded by working farmers, relative to realtors and to the public at large, as measured by RFR and FL, respectively.[12] In both specifications of the model the coefficients on these two

variables are positive and significant. It should be noted that the positive sign on FL can be taken as evidence that farmer/legislators are predominately small, family farmers. The importance of agriculture to total state income is related positively to the incidence of restrictive legislation, as expected, but the coefficient is insignificant. Finally, the estimates of POP and YPC provide unmistakeable support for the McCormick-Tollison analysis which suggests (1) the population is partially responsible for the level of economic regulation, and (2) the substitution effect dominates the income effect with respect to the manner in which per capita income affects regulatory activity.

IV

Concluding Comments

IT IS NOT ARGUED that the restriction of foreign purchase of U.S. farmland has not been produced by a complex of motives of the special interests involved. What has been argued is that owners of small, family farms are net demanders of farmland, and that, because low prices of land enable them to make greater gains from their farm operations, they have attempted to depress land prices. They have been successful at doing so by using the power of their numbers to obtain legislative restrictions which bar foreign investors from the farm real estate market.

The net effect of these restrictions is to transfer wealth from large farmers to small, family farmers. The resulting distribution of resources may be wasteful, in the strict economic sense, if foreign owners would produce commodities of greater value from the land than family farmers do now.[13] Since votes count heavily in determining legislative outcomes, and large farmers have few votes and foreigners have no votes, the political process may transmit preferences inefficiently under specified conditions. Votes are an inaccurate reflection of intensity of desire. Thus, the restriction of foreign ownership of farmland is an accomplished fact, but of questionable economic efficiency.

Notes

1. Even though only half of the states restricted alien ownership of real estate significantly as of early 1981, virtually all have debated bills which have introduced such restrictions.

2. It should be noted that the optimum size of family farms varies in different parts of the country depending on various conditions (crops, soil, climate, etc.).

3. *Foreign Investment in the United States,* Practising Law Institute Course Handbook Series, No. 297 (1979), p. 352.

4. *Ibid.*

5. Peter M. Blau and Otis D. Duncan. *The American Occupational Structure* (New York: John Wiley and Sons, Inc., 1967), p. 39.

6. Letters received by the author, from the offices of the Secretaries of State and the Attorneys General for the 50 states invariably cite the danger to family farmers as a motivation for passage

of farmland restrictions. One particular reply proved illuminating: "The enclosed bill, introduced during the 130th General Assembly (1979–80), . . . was approved by the House but not by the Senate and so did not become law. The sponsor, Rep. William T. Brady, himself a farmer, was up in arms. But he ran into difficulties when a couple of *large local farmers whose lands were coveted by aliens at Xmas prices objected to anyone telling them how or when they could sell.* Thus greed won out over foresight." (emphasis added)—from a letter by Jack Gibbons, Legislative Council, Dover, Del. (March 13, 1981).

7. Robert E. McCormick, and Robert D. Tollison, "Wealth Transfers in a Representative Democracy," in *Toward a Theory of the Rent-Seeking Society,* edited by J. M. Buchanan, R. D. Tollison and G. Tullock (College Station: Texas A & M University Press, 1980).

8. Realtors, since they work on commission, have an obvious vested interest in maintaining as much competition for farmland as possible.

9. Such restrictions normally take one of two forms: direct restrictions regarding the quantity of acreage that a foreign alien may obtain legal title to, and time limits on holdings. The effect of the latter regulation is to drive up the cost to aliens of holding land, thus reducing the profitability of investment, shifting the total demand for farmland down. South Carolina has an official acreage restriction of 500,000 acres which is treated as a non-restriction, since it is nonbinding—no NRA comes close to owning even one-tenth of that amount.

10. McCormick and Tollison, *op. cit.,* p. 296.

11. *Ibid.*

12. The "public at large" refers to speculators, other potential investors in farmland, and the consuming public, whose wealth is affected by the assignment or reassignment of property rights to farmland. Moreover, these groups all compete for the legislature's valuable time, and time spent considering farmland regulation is time not spent evaluating some other interest group's personal wealth-enhancing proposal.

13. In the socioeconomic sense, however, a majority of citizens may feel that it is good public policy to favor the family farm as against the corporation farm. This issue is not examined here.

Two Studies of the Welfare State

PETER KOSLOWSKI, PHILIPP KREUZER and Reinhard Löw have edited a collection of studies, *Chancen und Grenzen des Sozialstaats* (Chances and Limits of the Welfare State), which investigates the foundation of the Welfare State and the causes of its financing problems. The collective effort seeks to work out new perspectives for the development of State and society, using the analytical tools of philosophy, law and sociology. Published by J. C. B. Mohr (Paul Siebeck) in Tübingen, West Germany, the price is DM 38.

The crises of crisis management is a theme that runs through *Contradictions of the Welfare State* (Boston: MIT Press, 1984, $12.50 paper, $30 cloth), a collection of the essays of the German social scientist, Claus Offe. He investigates why, in the present period, the capitalist Welfare States are no longer capable of dealing with their socio-political problems and conflicts. He discusses the viability of the proposals for restructuring the Welfare State coming from the New Right, the corporatists and from the democratic socialists.