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## TOP 10 ISSUES IN AGRICULTURAL LEASES FOR LANDLORDS AND TENANTS

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## TOP 10 ISSUES IN AGRICULTURAL LEASES FOR LANDLORDS AND TENANTS

### 1. DUE DILIGENCE

#### A. Economic Issues.

- i. Landlord: Can the tenant afford to pay the rent and perform its lease obligations. Credit check. Tenant financials. Guarantor.
- ii. Tenant: Can the landlord afford to perform its lease obligations. Does the landlord own the leased property and equipment? Is the property collateral for a loan? SNDA.

#### B. Condition of Land, Buildings and Equipment.

- i. Tenant: Perform inspections of leased property and equipment.
- ii. Landlord: Should disclose any known material defects.

#### C. Environmental.

Background: Under various state and federal laws, both “owners” and “operators” of real property contaminated by hazardous waste or hazardous substances are generally jointly and severally liable for the entire cost of remediation, regardless of fault. Although there are exceptions, the exceptions are construed narrowly, and it is therefore essential that adequate environmental investigation be undertaken.

Phase I environmental site assessment or ESA: This is a study conducted by the environmental consultant of all public records and background information concerning the use of the property, the adjacent properties, and any hazardous waste release that has occurred in the vicinity of the property. A report is typically prepared that will provide a recommendation of any further study or testing. By definition, a Phase I ESA does not include testing of soil, water or air samples.

ESA Phase II: This is a study that includes soil, ground water, and/or air samples. If contamination is found, a report on a Phase II ESA will typically provide recommendations for remediation.

- i. Tenant: The tenant should complete whatever environmental investigation the tenant chooses before leasing the property, particularly for properties in or near industrial areas or with a history of pesticide, herbicide or other hazardous material usage.
- ii. Landlord: The landlord will want to make sure the tenant is obligated to provide a copy of any Phase I ESA report to the landlord, and have control over the performance of any Phase II testing. If landlord is willing to allow a Phase II, consider addressing the following: (i) scope of Phase II must be approved by landlord, (ii) results of Phase II are confidential except if disclosure is required by law, (iii) retain approval rights for

environmental consultant, and (iv) require tenant to indemnify and hold landlord harmless for any damage done as a result of the Phase II.

**D. Water Rights.**

i. Tenant: If tenant's agricultural operation will use water, the availability of water and right to such water should be verified. When there are or may be water rights associated with a property being leased, a water rights evaluation should be undertaken as part of the due diligence process. This may include:

- (1) Review of the applicable permit or certificate to understand the terms and conditions of the water right, and to confirm that the prospective landlord actually owns the water right.
- (2) Compare the permitted or certificated use to the actual use being made of the water (they should be the same).
- (3) Review any agreements related to the landlord's water right. A common example is an easement or license agreement to access irrigation equipment, pumps and wells associated with the water right.

ii. Landlord: Landlord should be prepared to provide documentation of its water rights.

iii. Water Rights Red Flags:

- (1) Is your prospective landlord using water without a water right or inconsistent with a water right?
- (2) Is there a water right owned by your prospective landlord without water actually being used?

E. **Survey.** Allows parties to clearly delineate and define the leased premises. Rent may be based on confirmed acreage. Avoid boundary line disagreements. Confirm access and any easements encumbering premises.

**2. THE LEASE AGREEMENT**

“Standard” forms for agricultural leases not generally available. Often primarily commercial in nature, but may contain residential elements if a dwelling is included. In many states, commercial leases generally unregulated and residential leases highly regulated.

A. Landlord: Typically desires higher level of detail in describing the parties' respective rights and obligations, and protective of the landlord, which often yields a longer,

more formal agreement. If both commercial and residential components involved, consider separate lease agreements for each and make them cross-contingent.

- B. Tenant: Typically required to use the landlord's lease form. Goal of tenant's counsel is to make necessary and appropriate modifications to create fair and balanced agreement in light of current market conditions.

### **3. RENT**

- A. Base Rent: Should be clearly specified, or capable of quantification if based on production, acreage or other measure.
- B. Adjustments: Specify timing and method of calculation – fixed percentages, CPI or other measure.
- C. Expenses: Clearly specify which party pays the property taxes, assessments, utilities and insurance premiums, and how such expenses will be paid.
- D. Rent typically payable without offset or deduction. Tenant may attempt to negotiate for self-help right and ability to offset costs in event of landlord failure to perform.

### **4. USE OF THE PREMISES**

- A. Landlord: Confirm any specific conditions to use (e.g. organic). Generally confirm use of good farming practices, no commission of waste. Seek broad indemnification of landlord for any issues caused by tenant's use.
- B. Tenant: Seek flexibility in use, specify use of pesticides and herbicides in compliance with labeling and applicable law. Seek to limit indemnification to a reasonable scope (e.g. "except to the extent caused by landlord").

### **5. CONDITION OF THE PREMISES; MAINTENANCE AND REPAIR**

- A. Landlord: Typically AS IS, except for any express warranties. Obligations to maintain and repair, if any, may include well/pump equipment, structure, foundation and roof of improvements. Landlord may have statutory or common law obligations with respect to residential dwelling on the property.
- B. Tenant: Attempt to obtain warranties from landlord - compliance with laws, condition of buildings and equipment. Any improvements or repairs promised by landlord should be specified in the lease. Should attempt to have the landlord perform maintenance and repairs of a capital nature and only pay for an amortized portion applicable to the lease term.

Both parties benefit from reasonably detailed documentation of the condition of the leased property and equipment at the commencement of the term.

## **6. ALTERATIONS DURING THE TERM**

- A. Landlord consent required? What is the standard for landlord consent – sole discretion v. reasonableness?
- B. Ownership of alterations? Obligation to remove at end of lease term?

## **7. ASSIGNMENT AND SUBLEASING**

- A. Landlord consent required? What is the standard for landlord consent – sole discretion v. reasonableness? Common carveouts.
- B. What process and documentation are involved?

## **8. DEFAULT AND REMEDIES**

- A. What constitutes a “Default”? Differentiate from “breach” or “violation”.
- B. Notice and opportunity to cure essential protection for tenant. A clear and unambiguous notice provision should be included that tells the parties how notice is to be given, to whom it is to be given, and when notice is effective.
- C. Landlord right to evict and retake possession by legal process or self-help, if available.
- D. Landlord’s right to dispose of the tenant’s personal property and equipment. Tenant may have financing, so consider agricultural lien and priority. Right to harvest considerations.

## **9. ALTERNATIVE DISPUTE RESOLUTION**

- A. Mediation: May be required by lease or elected by parties. Any resolution reached is voluntary. Facilitated by private mediators, dispute resolution services, or governmental agencies.
- B. Arbitration: May be required by lease or elected by parties. Arbitrator will impose a binding resolution on the parties. Similar to expedited, private trial.

## **10. SPECIAL AGRICULTURE CONSIDERATIONS**

- A. Right to Harvest: ORS 91.230 – “When the leasing or occupation is for the purpose of farming or agriculture, the tenant or person in possession shall, after the termination of the lease or occupancy, have free access to the premises to cultivate and harvest or gather any crop or produce of the soil planted or sown by the tenant or person in possession before the service of notice to quit.”
- B. Hemp and Marijuana – Marijuana remains illegal at the federal level. Require tenant compliance with state-specific licensing requirements (marijuana and hemp have different licensing requirements). Will need to be able to show zoning compliance, water right availability, security plan, etc. Immediate termination in the event of federal criminal enforcement actions (marijuana).