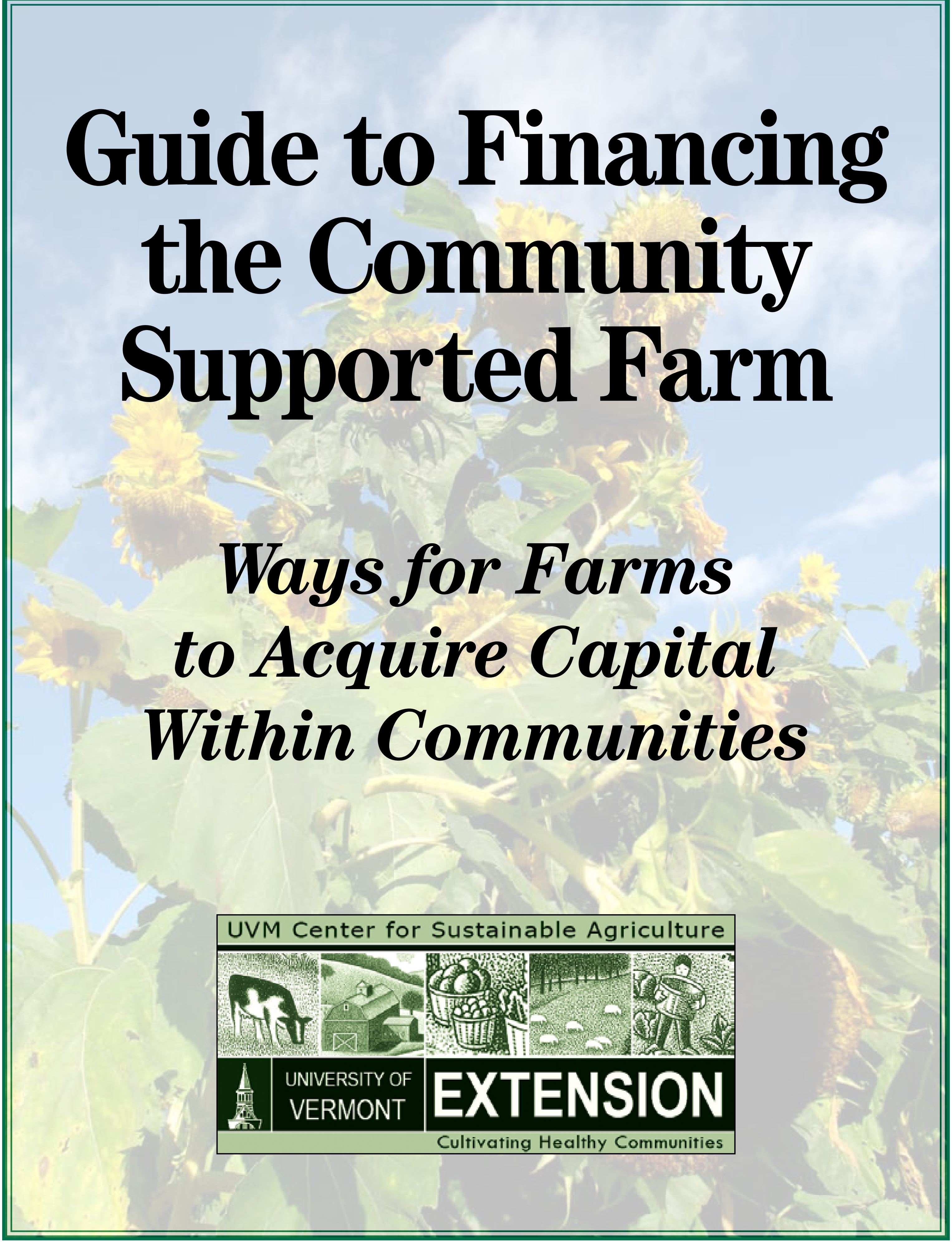

Guide to Financing the Community Supported Farm

Ways for Farms to Acquire Capital Within Communities

UVM Center for Sustainable Agriculture
UNIVERSITY OF VERMONT EXTENSION
Cultivating Healthy Communities

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Acknowledging with gratitude the contributing authors and members of the guide review team:

Matthew Burke, Owner and Farmer, Bloomfield Farm
Anthony Iarrapino, Esq., Staff Attorney, Conservation Law Foundation
Mark Cannella, Farm Business Management Specialist, University of Vermont Extension
Emily Curtis-Murphy, Owner and Farmer, Fair Food Farm
Annette Higby, Esq., Attorney-at-Law
Beth Holtzman, New Farmer Project Coordinator, University of Vermont Extension
Walter Jeffries, Owner and Farmer, Sugar Mountain Farm
Josh Jerome, Loan Officer, Community Capital of Vermont
James Macon, Founder and Principal, Barbour Alliance, L3C
Kristina Michelsen, Esq., Attorney-at-Law
Ken Merritt, Esq., Attorney, Merritt & Merritt & Moulton
Kenneth Miller, Esq., Attorney, Law for Food, LLC
Matt Mole, Success on Farms Program, Intervale Center
Keith Morris, Owner and Farmer, Willow Crossing Farm
Mary Peabody, Community and Economic Development Specialist, University of Vermont Extension
Corie Pierce, Owner and Farmer, Bread and Butter Farm
Erin Roche, Research Specialist, University of Vermont Center for Rural Studies
Rachel Schattman, Owner and Farmer, Bella Farm
Elizabeth Spellman, Law Clerk, Conservation Law Foundation
Janice St. Onge, Deputy Director, Vermont Sustainable Jobs Fund
Ben Waterman, New Farmer Project, University of Vermont Extension Center for Sustainable Agriculture
Cathy Yandow, Communications Support Specialist, University of Vermont Extension

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INTRODUCTION

by Ben Waterman, New Farmer Project, University of Vermont Extension Center for Sustainable Agriculture

Increasing numbers of farmers are exploring creative ways to acquire capital for farm operations.[1]

The following pages detail options and considerations for crafting unconventional financial arrangements that have been used in other sectors of the economy, but might be new to the agricultural sector. We guide the reader through basic legal issues relevant to farmers and community members when pursuing these arrangements. We highlight several mechanisms that allow for creativity and customization of financial transactions at the neighbor-to-farmer or farmer-to-community-member level:

- the promissory note
- the owner-financed land sale,
- equity financing
- revenue-based financing
- the "multi-year" CSA
- share leases

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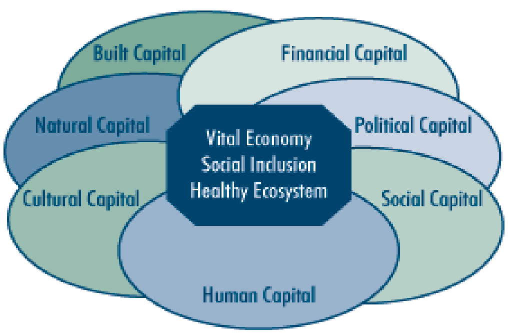
Four farmers who have tested these and other alternative ways to source capital for farm operations have written case studies included throughout this guide.

This guide defines ***Community Supported Farm*** as a farm whose financial and social support comes from individuals or entities in surrounding communities. Like-minded individuals with common interests make up communities; they are not necessarily geographically-based. For purposes of this guide, **Community Financing** is financial capital exchanged directly between farmers, food processors and people or other entities within their communities. **Community Capital** includes human, environmental and financial capital.[2] While this guide focuses on financing mechanisms, its premise is that all forms of capital are equally important to sustainable and flourishing communities.



Seven types of capital, all integral to community vitality.[2] Image used with the permission of Dr. Cornelia Flora, Department of Sociology, Iowa State University

This guide outlines ways in which community financing can be transferred, often with flexible terms that enable farmers to acquire capital for farm operations. This might include capital assets such as food processing equipment and energy-efficient infrastructure. Other uses of community financing might include securing short-term operating cash; making improvements to product quality; enhancing soil and water quality, preserving working landscapes; hosting social events; and providing other benefits. Community financing's fundamental purpose is to enable the creation of products and services for the benefit of the community. In a sense, the equation can come full circle. **Where there is a Community Supported Farm, there also can be a Farm Supported Community.**

This guide is designed to address questions that farmers might have, but anyone hoping to become more engaged in building community capital will find it informative. It provides case studies and replicable models of innovative farmers who have utilized community financing. It outlines key talking points for communicating possibilities, negotiating, and developing sensible community financing agreements.

This publication covers important legal issues relevant to crafting customized financing arrangements. It is by

1 Anecdotally evident, since the financial crisis of 2008, by the private sector taking interest in farms and food ventures as potential investment vehicles, and farmers seeking investors through various avenues, such as through "Entrepreneurial Showcases" at investor conferences and gatherings (example: "Slow Money National Gathering").

2 Iowa State University Department of Sociology researchers Cornelia and Jan Flora along with Susan Fey developed the Community Capitals Framework, first presented in their 2004 book, *Rural Communities: Legacy and Change* (2nd ed.). Boulder, CO: Westview.
Press. Descriptions of the seven capitals: human, social, natural, financial, built, cultural, political can also be found at: http://www.soc.iastate.edu/staff/cflora/ncrcrd/capitals.html or at http://edev.byu.edu/ellsymposium/documents/community_capital.pdf.

Above image used with the permission of Corie Pierce.

no means intended as a substitute for the counsel of qualified tax accountants and attorneys. In fact, these services may become essential when developing unique, customized community financing arrangements. This guide's purpose is to empower farmers and community members with knowledge of pertinent issues and potential options. In turn, it might be possible to reduce legal and accounting costs by calling on the service of outside experts only when it is most appropriate.

The interest in community financing at the time of this writing is expanding.[3] While there is much work to be done, this guide does not explore policy level considerations, such as towns setting aside common land for community farms. ***The purpose of this work is to provide easy-to-read, timely and relevant information outlining options and considerations for exploring and crafting creative financing arrangements for community supported farms. While the following pages contain many references to ways in which parties to an agreement can reduce liability risk, again it cannot be overemphasized: The information provided is for educational purposes only, and is not a substitute for sound legal representation from a qualified attorney.***

Finally, financing mechanisms presented in the following pages are highlighted as "complementary" rather than "alternatives" to traditional debt financing. This guide does not contain information on bank loans, USDA Farm Service Agency (FSA), institutional agricultural credit programs, or other forms of traditional debt financing. Farmers are encouraged to contact agricultural lenders for more information on existing loan programs. Many local avenues of traditional debt financing can, in fact be considered "community financing" as defined in this guide. Local agricultural finance experts can provide valuable technical assistance with farm business management planning and help farmers develop appropriate farm finance strategies. They are a tremendous resource that should not be overlooked.

The financing models in this guide might be new to the agricultural sector, but they have been time tested through decades of use in other sectors of the economy as innovative ways to fund business start-up and early growth stages. In the same manner farmers have refined pioneering practices in production systems, it might only be a matter of time before they adopt practical innovations in financing.

For more background information on community financing, see Appendix 1 of this guide: Community Financing Theory: the Role of Patient Capital in Sustainable Agriculture and Rethinking Profit and Return on Investment. The following chapters detail practical options and considerations for community financing of farms. Topics include:

- Securities regulations and why they are important
- Acquiring land through owner-financed sales and land contracts
- Talking points for dealing with farmland investors
- The promissory note
- Equity financing
- Revenue-based financing
- The multi-year CSA share
- The share lease
- A comparison of business structure in terms of raising capital

Four case studies are also included throughout this guide. They are written by farmers who have utilized various forms of community financing or who are exploring these kinds of arrangements.


Image used with the permission of Walter Jeffries. ©2012 Walter Jeffries, SugarMtnFarm.com.

3 Anecdotal evidence based on the author's numerous conversations in 2010-2011 with Cooperative Extension agricultural educators and other agricultural service providers.

PREFACE:
Matching Financing with Appropriate Use

By Mark Cannella, Farm Business Management Specialist, University of Vermont Extension

Farms may arrive at alternative community financing opportunities for a variety of reasons. Before seeking credit or finance from other sources it is important to consider the basic reasoning why a business needs capital and what is required for such a relationship to exist. Farm owners will need to identify their annual operating expenses and proposed multi-year capital investments separately in order to evaluate the best financing option. There is a difference between seeking operating capital versus investment capital.

Farms need cash to pay for annual operating expenses before cash receipts from products sales are received. Farms may need a large amount of borrowed cash for the first year of operation and they will likely require a certain amount of cash every year at the beginning of the season. Operating expenses include everyday expenses to purchase the inputs that keep the business running over the course of the year. This includes items like advertising, seeds, fertilizer, fuel, labor payroll, broiler chicks (to be sold within the year), insurance and utilities. A business strives to pay off its annual operating expenses within the year before it begins to accrue expenses for the next year. Ideally, all bills are paid off and any sources of credit/finance for operations have been paid off from farm income received that period.

Farms will also need finance options to make capital investments or acquire assets that keep the farm running. These investments, by definition, will have a multi-year life span and include items like: machinery, breeding livestock, conservation improvements, buildings and land. Finance options for investments are structured to reflect the cost, the lifespan and income generating potential of asset. For example, a tractor or construction improvement has a shorter useful lifespan and lower cost than a large tract of farmland. A tractor loan would commonly be paid back over two to seven years, while investments in real estate would be expected to be paid down over many more years. Real estate mortgages, for instance, may range from 20-35 years.

Each source of capital comes with certain obligations, relationships and maintenance. The level of obligation, type of relationship and amount of maintenance will vary among different sources. Business owners will decide which sources match their preferences or requirements. This guide provides examples of many benefits to community finance options. Owners should consider that there are costs, however, associated with alternative finance options that may not be apparent at the onset. Two significant costs can include the time required to organize the agreement and the likely need for professional services (legal or tax accounting) to establish, verify or properly report on the agreement. These costs may or may not outweigh the benefits of a community finance option. Owners should consider these costs when engaging in community finance relationships to make sure they have the time and resources to properly execute and administer the process from start to finish.

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"Shiitake Mushroom Log Laying Yard." Image used with permission of Ben Waterman.