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**Diversifying the Farm Enterprise: Alternative  
Land Use and Land Tenure Law in the UK**

by

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# DIVERSIFYING THE FARM ENTERPRISE: ALTERNATIVE LAND USE AND LAND TENURE LAW IN THE UK

*Christopher P. Rodgers\**

## I. AGRICULTURE IN THE 1990s—CHANGING PRIORITIES

The agricultural policies pursued after the war in the United Kingdom (UK) were intended to maximize production and to provide a reliable food supply at reasonable cost. The success of post-war policy, enhanced since the UK joined the European common agricultural policy, has led in turn to new problems—principally the need to address serious overproduction and the need for greater environmental control over certain agricultural practices. This has in recent years led to a reassessment of priorities, and the introduction for the first time of measures intended to take land out of production. The 1992 reform of the CAP introduced substantial reductions in price support and subsidies for agricultural produce. In the arable sector, the set aside of land from production is now a precondition for the receipt of subsidies under the arable area payments scheme. At the same time, environmental controls are being integrated more fully into agricultural support policies. Falling agricultural prices, and the reduction of subsidies, serve to highlight the need for diversification of farm enterprises into nonagricultural business ventures if a vibrant rural economy is to be sustained. A number of government schemes have been used to offer incentives to diversify. Some of the diversification encouraged includes farm shop retailing, equestrian centers, and the development of wildlife and educational centers. The Farm Diversification Scheme of 1987, for example, made capital grants available to farmers seeking to diversify into a number of nonagricultural activities. This scheme has now closed, and the emphasis under its successor—the Farm and Conservation Grant Scheme of 1991—was more on grant aid for conservation work in the countryside. Similarly, the pilot set-aside scheme in the UK offered grant aid for farmers to set land aside to nonagricultural use, such as golf courses and educational projects. Grants for diversification are not available, however, under its successor since 1992, the European Arable Area Payments scheme.

Although financial subventions have been made available for diversification projects, this in no way implies exemption from the normal requirements of land use law. Any diversification which involves the erection or modification of buildings for nonagricultural use on a farm may require planning consent from the local planning authority. In considering applications for development consent, however, the planning authority is likely to view favorably applications to develop viable nonagricultural business

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ventures in the countryside. The most recent official policy guidance on planning matters involving nonagricultural use on former farmland neatly encapsulates the new priorities:

The increasing efficiency of agricultural production and changes in agricultural policy mean that retaining as much land as possible in agricultural use no longer has the same priority. The priority now is to promote diversification of the rural economy so as to provide wide and varied employment opportunities for rural people, including those formerly employed in agriculture and related sectors.<sup>1</sup>

Difficult legal problems may also arise when the producer wishing to diversify occupies his holding entirely (or partially) as a tenant. Farm tenants enjoy considerable security of tenure, and additional statutory rights including rights to compensation for improvements, freedom of cropping, removal of fixtures, and rent review. Lifetime security of tenure was introduced by the Agricultural Holdings Act of 1948 (1948 Act), and extended in 1976 by legislation conferring succession rights on close relatives of a tenant entitling them (subject to qualifying conditions) to succeed to the tenancy on the tenant's death.<sup>2</sup> The legislation was consolidated in the Agricultural Holdings Act 1986 (1986 Act). The 1986 Act reflects the post-war philosophy of agriculture in the structure of protection it affords farm tenants. Security of tenure is made conditional on the tenant maintaining an efficient form of agricultural production, and the presupposition is that the land (or at least the majority of it) will be used solely for agricultural purposes. This philosophy is written into the fabric of the legislation in a variety of ways and is examined further below. A tenant wishing to diversify into nonagricultural business use could face a number of problems, including the possibility that the protection of the 1986 Act might be lost altogether if substantial diversification takes place and the character of the holding ceases to be agricultural. The potential impact on the tenant's legal rights would clearly constitute a disincentive to effective diversification.

It is self-evident that this runs counter to the modern emphasis on creating a broadly based rural economy. The structure of land tenure law has, therefore, been recast in the Agricultural Tenancies Act of 1995 (1995 Act) by the creation of a new type of farm tenancy—to be known as the “farm business lease”—with the intention of providing an appropriate legal medium for diversification by tenant farmers, while at the same time encouraging a revival in the tenanted sector by removing restrictions on farm lettings. The 1995 Act will only apply, however, to tenancies granted on or after September 1, 1995. The 1986 Act and its more restrictive regime will continue to apply to all farm tenancies granted before this date. To have an overall assessment of the legal regime governing land tenure and diversification, it is necessary to

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1. PLANNING POLICY GUIDANCE NOTE 7, THE COUNTRYSIDE AND THE RURAL ECONOMY ¶ 2.3 (1992).

2. See Agriculture (Miscellaneous Provisions) Act, 1976, Part II (Eng.). These provisions are now contained in Part IV of the Agricultural Holdings Act of 1986. These succession rights have, since 1984, also applied on the retirement of a tenant.

look initially at the legal position for tenants with 1986 Act tenancies, before considering the reforms introduced by the 1995 Act. The existence of two generation-succession rights will ensure that a large number of 1986 Act tenancies will remain in being for many years to come, whatever the merits of the reforms.

## II. AGRICULTURAL HOLDINGS—THE AGRICULTURAL IMPERATIVE

The Agricultural Holdings Act of 1986 contains a detailed code of rights for farm tenants, for example, security of tenure, compensation on termination of tenancy, rights to remove fixtures, freedom of cropping, and rent reviews. These rights are variously conditioned, however, by the supposition that the tenant must maintain a reasonable standard of husbandry on the holding, given the fixed equipment provided by the landlord and the character and situation of the farm. Diversifying into nonagricultural activities can have a number of consequences for the tenant's legal position under the 1986 Act. If diversification is extensive, the holding might legally cease to be an agricultural holding at all. If the holding legally ceases to be an agricultural holding, the protection of the 1986 Act and its attendant rights will be lost altogether. Even if diversification is not this extensive, it may still affect the way in which the tenant's statutory rights apply. In some cases, the statutory rights may work to the tenant's disadvantage.<sup>3</sup>

### A. Protected Status—Agriculture or Business?

It may be of some comfort to the farmer considering diversification to know that the draftsmen of the 1986 Act clearly contemplated *some* nonagricultural use of land in a farm tenancy. The draftsmen provided for this in section one of the Act which defines an agricultural holding and the scope of protection afforded by the Act. The difficulty is determining how much non-agricultural use will be possible before the character of the tenancy itself ceases to be "agricultural"; for if the character of the holding, viewed as a whole, ceases to be agricultural, then the tenancy will lose its protection under the 1986 Act. This will have severe consequences for the security of tenure of the farmer and entail the loss of other rights, such as the right of his close relatives to succeed to the tenancy on his death. The Court of Appeal held in *Hickson & Welch Ltd. v. Cann*<sup>4</sup> that if agricultural use is abandoned by the tenant, with or without the consent of the landowner, then notwithstanding the terms of the tenancy agreement the tenancy will cease to be an agricultural holding.<sup>5</sup> The tenant can, in other words, unilaterally abandon the protection

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3. For discussion of various issues under the tenancy legislation occasioned by alternative land use see also, inter alia: Michael Cardwell, *Legal Issues of Alternative Land Use*, in NATURE CONSERVATION AND COUNTRYSIDE LAW Chapter 9 (Christopher P. Rodgers ed., Univ. of Wales Press 1996); Michael Cardwell, *Set Aside Schemes and Alternative Land Uses: Some Problems for the Tenant Farmer*, 56 CONV. & PROP. LAW. (n.s.) 180 (1992); Hume Hargreave, *Diversification: Problems for the Tenant Farmer*, 134 SOL. J. 1032 (1990).

4. *Hickson & Welch Ltd. v. Cann*, 39 P. & C.R. 218 (1977).

5. *Id.* at 220-21.

of the 1986 Act. Tenants considering diversification will need to weigh carefully this possibility when considering the options available to them. If the farm comprises both freehold and tenanted land, for instance, it may be advisable to locate diversified farm-based business activities on freehold land and continue traditional agricultural production on the tenanted portion of the holding. Where the holding is wholly tenanted, the farmer will need to carefully consider the extent of diversification and the need to protect the "agricultural" character of the tenancy. The farmer may derive some comfort from the fact that the courts have, in this context, viewed diversified enterprises with considerable generosity.

By virtue of section one of the 1986 Act, a tenancy is an agricultural holding if the *aggregate* of the land let is let under a contract which is an agricultural tenancy. Qualification of a contract as an agricultural tenancy is determined by the terms of the tenancy, the actual or contemplated use of the land at the time of letting and subsequently, and "any other relevant circumstances."<sup>6</sup> This is subject to a very important qualification: the tenancy will be agricultural only if the whole of the land let is so let for use as agricultural land *subject to such exceptions as do not substantially affect the character of the tenancy*.<sup>7</sup> Some nonagricultural use is possible without affecting the character of the tenancy, but the *substantial* use must remain agricultural. If the substantial use remains agricultural, the entire holding will be protected by the 1986 Act, because the courts have refused to contemplate severance of nonagricultural land where the predominant use, viewed overall, remains agricultural. In the leading case of *Howkins v. Jardine*,<sup>8</sup> Lord Justice Jenkins gave the following formulation of the applicable test, which still holds good:

[O]ne must look at the substance of the matter and see whether, as a matter of substance, the land comprised in the tenancy, taken as a whole, is an agricultural holding. If it is, then the whole of it is entitled to the protection of the Act. If it is not, then none of it is so entitled.<sup>9</sup>

After September 1, 1995, it is not possible to grant a tenancy of an agricultural holding under the 1986 Act. The chief import of the "substantial use" test developed by the courts will be the issue regarding whether tenancies which were clearly agricultural holdings at the outset remain so, and whether statutory protection has been abandoned consequent upon diversification into nonagricultural business enterprise by the tenant.

Where the tenancy was an agricultural tenancy at the commencement of the tenancy, the *substantial* use must remain agricultural if statutory protection is to continue. The courts have, however, interpreted the substantial use

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6. Agricultural Holdings Act, 1986, § 1(2) (Eng.).

7. *Id.*

8. *Howkins v. Jardine*, 1 K.B. 614 (1951).

9. *Id.* at 628; see *Lord Monson v. Bound*, 1 W.L.R. 1321, 1324 (1954) (holding that land let to a tenant for horticulturist purposes, but which contained a retail shop, glass conservatory to display flowers for sale, wreath-making room, greenhouses, and only one-third of the land cultivated, did not constitute an "agricultural holding" because the tenancy as a whole was not in substance a tenancy of agricultural land).

test liberally when considering cases of alleged abandonment of agricultural use, usually consequent upon diversification. For example, in *Wetherall v. Smith*,<sup>10</sup> the court held that the relevant period for deciding whether agricultural use has been abandoned is the time period immediately prior to the service of a notice to quit, ending the tenancy.<sup>11</sup> Further, the court held that evidence of a settled intention to abandon agricultural use of the land is required and suggested that the abandonment of agricultural use for at least two years prior to notice to quit would be required.<sup>12</sup> It was not clear on the facts of *Wetherall* that the agricultural use had been abandoned sufficiently where land let for grazing horses and cattle was being used at the time of notice to quit for training and jumping horses in a riding school. A further complication is caused by the fact that an agricultural holding can cease to be protected if the land is still used for "agricultural" purposes, but not in connection with a trade or business, for example, if rented fields are used to graze recreational ponies free of charge.<sup>13</sup>

The most difficult situation arises when the land continues to be used for the purposes of a business, but the character of the *business* ceases to be agricultural if the activities generating the income of the business (or much of it) cease to be agricultural. This was the position in the leading case of *Short v. Greeves*.<sup>14</sup> The producer in *Short v. Greeves* rented a garden center extending to only 6.2 acres, and initially sold mainly plants raised on the holding. The site was fronted by a greenhouse, part of which was used for retail sales and a display area for home grown conifers and roses in containers. The area devoted to the retail operation was just over one acre. The retail operation developed considerably over time and was enhanced by the sale of garden equipment and plants purchased wholesale. The remainder of the holding, previously devoted to growing plants for sale, fell into desuetude. By the time the litigation arose, the proportion of the garden center's business turnover derived from the sale of home-grown plants had fallen to approximately forty percent, and sixty percent of the business turnover was derived from purely "retail" sales of goods bought in wholesale from elsewhere. The legal issue was whether the tenancy was that of an agricultural holding protected by the 1986 Act, or (as the landlord contended) a business tenancy within the scope of Part II of the Landlord and Tenant Act of 1954. The court, in finding the tenancy to be that of an agricultural holding, endorsed the presumption against a holding which is clearly agricultural at the outset ceasing to be such, without clear evidence of its substantial use ceasing to be agricultural.<sup>15</sup> But what exactly is meant by "agricultural use"? Section one of the 1986 Act directs one to consider not only the use of the land itself and the terms of the tenancy, but also "any other relevant circumstances."<sup>16</sup> The

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10. *Wetherall v. Smith*, 1 W.L.R. 1290 (C.A. 1980).

11. *Id.* at 1297.

12. *Id.* at 1297-98.

13. Agricultural Holdings Act, 1986, § 1(4)(a) (Eng.).

14. *Short v. Greeves*, 1 E.G.L.R. 1 (C.A. 1988).

15. This presumption is derived from the decision in *Wetherall v. Smith*, 1 W.L.R. 1290 (C.A. 1980).

16. Agricultural Holdings Act, 1986, § 1(2)(c) (Eng.).

court in *Short v. Greeves* held that turnover figures were relevant to determine the nature of the land use—agricultural or business.<sup>17</sup> But they are only one of a number of factors which must be balanced. The relative size of the areas of land used for agricultural and nonagricultural business use, as a proportion of the land leased in total, will also be relevant, as will the terms of the tenancy agreement itself. If the tenancy agreement prohibits nonagricultural use (as some traditional farm leases will) this may be decisive. Balancing the various criteria to ascertain whether agricultural use has been abandoned will not, in most cases, be easy. This is particularly the case as a small parcel of land used for a successfully diversified farm business, such as retail sales, will often generate a disproportionately greater income than agricultural use of the same land would. Where diversification occurs, therefore, it will often be difficult to predict with certainty whether the tenancy has remained agricultural (and protected) or not. In *Short v. Greeves* it was held, surprisingly perhaps, that sixty percent nonagricultural turnover was not sufficient to deprive the tenancy of its agricultural status.

This may provide some comfort to the farmer contemplating the diversification options for his holding. Complacency, however, should be avoided, as other cases have been differently decided on not dissimilar facts. In *Lord Monson v. Bound*,<sup>18</sup> for example, it was held that the tenancy of a florist shop, with greenhouses, was not an agricultural holding when only ten percent of the horticultural sales from the premises were of flowers grown there. Although the proportion of turnover from the respective parts of the enterprise will be relevant, it would seem that to outweigh actual agricultural use on the land let the turnover from nonagricultural sources must be very high. The difficulty of ascertaining the legal status of a diversified farm enterprise is further complicated in that the definition of an agricultural holding involves the resolution of several questions of fact. Whether the agricultural use of the holding is the *substantial* use is a question of fact. In the absence of a perverse decision, the higher courts will not interfere with a finding of fact at first instance on this central element of the definition. This will make it even more difficult, in many cases, to predict which side of the borderline between "agriculture" and "business" a decision will fall. A field used for grazing horses with occasional jumping and horse training has, for example, passed the substantial use test and been held to be an agricultural holding. By contrast, land used chiefly as a riding school with ancillary grazing and other agricultural activities has not been held to be an agricultural holding.<sup>19</sup> Notwithstanding the difficulties, however, the decisions in *Short v. Greeves* and *Wetherall v. Smith*, taken together, should provide some comfort for the farmer contemplating diversification. Where the character of the tenant's business use has changed, the tenancy will remain an agricultural holding unless it can be shown on the facts that a "substantial" proportion of the business turnover has been derived from nonagricultural sources of income

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17. *Short v. Greeves*, 1 E.G.L.R. 1 (C.A. 1988).

18. *Lord Monson v. Bound*, 1 W.L.R. 1321, 1324 (1954).

19. *Compare* *McClinton v. McFall*, 232 E.G. 707 (1974) *with* *Deith v. Brown*, 16 E.G. 513 (1956), *Bracey v. Read* [1963] Ch. 88, *University of Reading v. Johnson-Houghton*, 2 E.G.L.R. 113 (1985).

continuously for a period of at least two years. This may be difficult to prove in many cases.

Even if the protection of the agricultural legislation is not lost, there are other matters which farm diversification may affect. The security of tenure, compensation, and other rights conferred on tenants by the 1986 Act are based on the premise that the tenant should adhere to the standard of the reasonably competent farmer, given the fixed equipment provided by the landlord and the situation and character of the holding. In a number of cases, the continued exercise of statutory rights is conditioned on the maintenance of this standard. The standard, moreover, is defined in purely agricultural terms and makes no allowance for diversification or the wider economic view of rural business enterprise underlying modern government policy. This gives rise to a number of problems.

### B. *Good Husbandry—An Outmoded Standard*

The rules of “Good Husbandry” and “Good Estate Management” are set out not in the 1986 Act, but in the Agriculture Act of 1947.<sup>20</sup> As one might expect, the 1947 Act imposes standards which directly reflect the post-war preoccupation with maximizing agricultural production to reverse war-time food shortages, and promoting the development of an efficient agricultural industry for the post-war era. The sanctions for breach of the Rules of Good Husbandry were repealed in 1958.<sup>21</sup> They retain considerable importance, however, and adherence to the standards they demand is woven into the fabric of the Agricultural Holdings Act of 1986 in a number of ways. By virtue of section eleven of the 1947 Act, a tenant will be satisfying his duty to farm in accordance with the Rules of Good Husbandry if he is maintaining a reasonable standard of efficient production, having regard to the character and situation of the holding, the standard of management exercised by the landowner, and with a view to keeping the holding in good agricultural condition for the future.<sup>22</sup> A number of more specific factors to be considered are set out in section eleven, sub-section two.<sup>23</sup> For example, arable land must be cropped in a manner which maintains it in a good and clean condition of cultivation and fertility, and permanent pasture must be properly mown or grazed by livestock so as to keep it in good and fertile condition.<sup>24</sup> If the farm is a livestock enterprise, it must be properly stocked and an efficient standard of livestock management adopted.<sup>25</sup> Steps must be taken to keep livestock and crops free of disease and infestation by pests and insects, and harvested or lifted crops must be adequately protected.<sup>26</sup>

It will be immediately apparent that any farmer diversifying from traditional agricultural practice, or entering an environmental scheme which

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20. Agriculture Act, 1947, § 11(2) (Eng.).

21. Agriculture Act, 1958, § 10 and sched. 2, part 1 (Eng.).

22. Agriculture Act, 1947, § 11 (Eng.).

23. *Id.* at 11(2).

24. *Id.*

25. *Id.*

26. *Id.*

requires extensification of production, will run the risk of contravening the Rules of Good Husbandry. Taking good agricultural land out of production, even for sound environmental or business reasons, will be contrary to the rules unless justified by a *bona fide* agricultural reason, for example, the need to rotate arable cropping. Whether there has been a breach is assessed solely by reference to agricultural criteria and not wider business considerations. In the Scottish case of *Cambusmore Estates v. Little*,<sup>27</sup> there was a breach of the rules where the tenant leased out the whole of his milk quota and ceased dairy production altogether. The fact that quota leasing can produce a ready income and may be an appropriate utilization of farm assets was discounted. The court can only consider the facts in terms of agricultural production, and must assess whether a reasonably efficient standard of production is being maintained on the unit as a whole. When there is no production at all, this rule is breached, whatever the financial merits of leasing quota. The development of farm based businesses such as golf courses, go-cart tracks, riding schools, and the like will also *prima facie* breach the rules if carried out on tenanted land. Entry into one of the many environmental schemes now available may also cause problems. Putting land into non-rotational set aside for five years, under one of the environmental management options under the current European Union set aside arrangements,<sup>28</sup> for example, would run counter to the Rules of Good Husbandry—whereas set aside under the rotational option, which allows land to be set aside once every six years, probably would not. Similarly, reducing the stocking level of a livestock enterprise pursuant to an environmental management agreement (for instance in an Environmentally Sensitive Area) would also entail a technical breach of the rules.

Although not directly enforceable, the Rules of Good Husbandry are enforceable against a tenant by several indirect means. In the first instance, breach of the Rules may jeopardize the tenant's security of tenure. Schedule 3 of the 1986 Act lists eight "Cases" for possession, giving the landowner a right of statutory forfeiture—they apply, for example, where the tenant is in breach of the tenancy agreement or has been adjudicated bankrupt. Breach of the Rules gives the landowner the right to apply to an agricultural land tribunal for a Certificate of Bad Husbandry. If a certificate is issued, the landowner can then serve notice to quit under Case C. Obtaining a certificate is difficult, except in cases of extreme and obvious neglect, but if one is issued the tenant has no defense to a subsequent notice to quit and thus loses his security. In most farm leases adherence to the Rules of Good Husbandry is expressly incorporated as a term of the tenancy agreement. This has the effect of rendering Case D available to the landlord, who can then allege that breach of the Rules also constitutes a breach of tenancy. They can, therefore, be indirectly enforced by the service of a notice to remedy the alleged breach and, ultimately, by notice to quit. The tenant can, in this case, refer the

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27. *Cambusmore Estates v. Little*, 6 S.L.T. 33 (Scottish Land Court 1991).

28. The set aside rules are contained in the E.U. Arable Area Payments Scheme, established by Council Reg. 1765 of 1992. The management rules are implemented in the U.K. by the Arable Area Payment Regulations 1994, SI 1994/947. See Schedule 2 of the 1994 regulations for the detailed management rules applicable to both rotational and non-rotational set aside land.

breaches of tenancy to arbitration, and must be given a reasonable period to remedy the situation. The sole issue for adjudication by the arbitrator will be whether, on the facts, there *has* been a breach of tenancy. Wider issues of business efficacy are irrelevant.

The Rules of Good Husbandry also have a wider indirect relevance, in that many of the statutory rights and duties of landlord and tenant are qualified by reference to them. For example, when possession proceedings are brought under Cases D or E, alleging some breach of tenancy, the breach complained of must be one which is not inconsistent with the tenant's responsibilities to farm in accordance with the Rules of Good Husbandry.<sup>29</sup> This means that when there is a conflict between the standards set out in the Rules and the terms of the tenancy agreement, the Rules prevail.<sup>30</sup> Similarly, when the tenant can compel the landowner to provide fixed equipment on the holding, by applying to the agricultural land tribunal, his right to do so is dependent on him showing that what is requested is reasonable, regarding his responsibility to farm in accordance with the Rules of Good Husbandry.<sup>31</sup> Even if the landlord has no complaint as to the standard of farming practiced by the tenant, and no ground for using the forfeiture procedures in the Act, he can still serve a notice to quit and request the consent of the tribunal to its operation. One of the grounds on which consent is available is when "the carrying out of the purpose for which the landlord proposes to terminate the tenancy is desirable in the interests of Good Husbandry as respects the land to which the notice relates, treated as a separate unit."<sup>32</sup> This provision enables the landlord to apply for possession if he can prove that the land will be *better farmed* by him than under the stewardship of the tenant. To this end he will normally have to produce a scheme to show how he will improve the efficiency of the holding as a production unit. It is not necessary to show that the existing tenant is farming badly.<sup>33</sup> This procedure is infrequently used in practice, but its availability underlines the point that the overriding principle of the 1986 Act is to maximize the potential for efficient agricultural production on tenanted land.

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29. Agricultural Holdings Act, 1986, sched. 3, part 1 (Eng.).

30. *Id.*

31. *Id.* at § 11(1).

32. *Id.* at § 27(3)(a).

33. See *Davies v. Price*, 1 All E.R. 671 (1958) (stating there are two ways by which a landlord can gain possession: (1) by showing that the tenant is a "thoroughly" bad farmer, or (2) by serving a notice to quit and obtain consent to possession).

### C. Diversification—Whose Prerogative?

The tenant will face further problems if the diversification he proposes requires planning consent. Relatively minor development may require consent if buildings are to be erected or adapted for nonagricultural use, or if there is to be a material change of use of existing facilities from an agricultural to a non-agricultural use. A material change of use can occur where the ancillary uses to which land or buildings are put ceases to be agricultural, or where they cease to be ancillary to the primary agricultural use of the holding. Whether the link between the primary agricultural use of the holding and the ancillary use of particular buildings has been broken is decided by looking at the existing use of the planning unit as a whole. For example, selling farm produce grown elsewhere than on the subject holding will be a material change of use requiring planning permission, even if the proportion of "bought in" produce is small.<sup>34</sup> Selling farm produce grown on the holding will not. Similarly, diversification into animal trans-shipment by the creation of a lairage, or holding facility, for the storage and onward transport of livestock raised on other farms will require planning consent<sup>35</sup>—it would not for storage and transport of stock raised on the subject holding itself.

Planning consent can be applied for by the landowner, or even by a third party. Where planning consent is obtained, even for a limited diversification, this will give the landowner the right to serve notice to quit under Case B to Schedule 3 of the 1986 Act. The latter enables the landlord to give notice in two situations: where the land is "required" for a nonagricultural use for which planning permission has been granted on an application under the Town and Country Planning legislation, and where planning permission is not required for certain stated reasons, such as by reason of Crown immunity when the applicant is a government department. The policy of the 1986 Act is to confer protection on the tenant so long as the land is being used as agricultural land, but if it is no longer to be so used the parties once more have the rights given to them by the common law and the tenancy agreement.<sup>36</sup> If the tenancy agreement authorizes the resumption of possession of the whole or part of the farm for nonagricultural use on the giving of short notice, then the notice to quit can be shorter than the normal twelve months otherwise required by the 1986 Act.<sup>37</sup> If the landlord obtains planning consent for a diversified use, the tenant could lose possession of part, or all, of his holding and has little recourse other than to claim compensation for disturbance. The loss of even a small portion of land could cause considerable dislocation in the organization of the enterprise, such as when the land repossessed includes the farm buildings and fixed equipment.

The policy underlying Case B is that, as the owner of a capital asset (land), the agricultural landowner should be entitled to any increase in value

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34. *Williams v. Minister of Hous. & Local Gov't*, 18 P. & C.R. 514 (1967).

35. See *Warnock v. Secretary of State*, J.P.L. 590 (1980).

36. See the observations of Lord Cross in *Rugby Joint Water Board v. Footitt*, 1 All E.R. 1057 (1972).

37. Agricultural Holdings Act, 1986, § 25(2)(b) (Eng.).

that may accrue from possible development. The tenant has no defense to a notice under Case B, other than to challenge the veracity of the facts alleged by requiring arbitration. For example, a tenant may require arbitration as to whether the land is genuinely "required" for nonagricultural use, in the sense that the landlord has a present and settled intention to carry out the scheme authorized by the planning consent, and has the financial means to do so. The real issues for decision arise, therefore, at the earlier stage when the planning decision is made. The courts' attitude to the plight of the farm tenant faced with dispossession in these circumstances offers little encouragement. In *Fowler v. Secretary of State & North Wiltshire DC*,<sup>38</sup> the Berwick Trust applied for planning consent to develop one of its farms (Battlelake Farm) as an equestrian center. The tenants of Battlelake Farm objected, arguing that they would suffer disproportionate hardship if planning permission were granted in that they would have to quit the farm (because of the availability of Case B), and this would render adjacent land which they also farmed difficult to work because all the farm buildings were on the subject holding. On appeal, the court held that personal circumstances, such as hardship, might be a material consideration for the planning authority to consider, but the *weight* to be given to them was a matter for the decision-maker alone. The fact that notice of a planning application, by either the landlord or a third party, has to be served on a farm tenant does not require the decision maker to give greater weight to the fact that such a tenant might consequently be dispossessed from his holding as a result of the grant of permission than to any other set of personal circumstances.<sup>39</sup> The implications of the grant of permission for the tenant's security is one material factor which is to be weighed with other material consideration when deciding the application. The tenant's security of tenure will, in effect, be subordinated to the economic interests of the landowner in promoting diversification—unless exceptional hardship can be shown.

#### D. Succession to Farm Tenancies

When a farmer retires or dies, an application for a succession tenancy may be made by his son, daughter, or spouse. Under the statutory succession scheme in the 1986 Act, two transmissions of the tenancy can take place. The scheme applies only to tenancies granted before July 12, 1984, of which a considerable number remain. A tenancy with succession rights is a valuable commodity, to be jealously guarded, and the tenant intending to diversify should consider the implications for the operation of the succession provisions on his later retirement. To establish his eligibility to succeed to the tenancy, a son or daughter will have to show that his or her principal source of livelihood has been "derived from his agricultural work on the holding or on an agricultural unit of which the holding forms part."<sup>40</sup> His principal source of income must have been so derived, moreover, for a continuous period of

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38. *Fowler v. Secretary of State & North Wiltshire DC*, J.P.L. 365 (1993).

39. *Id.* at 368.

40. Agricultural Holdings Act, 1986, § 36(3)(a) (Eng.).

five years<sup>41</sup> out of the seven immediately preceding the tenant's retirement or death. To be the applicant's "principal" source of livelihood, drawings from the farm accounts must account for not less than fifty percent of the applicant's total expenditure on living expenses.<sup>42</sup> It is preferable for the potential applicant to draw income as an employee, rather than a partner in the business. If the applicant is a partner and the farming business is technically insolvent, the court may regard his "livelihood" as having been derived from the business overdraft and loans, rather than from his work on the holding.<sup>43</sup> It should also be appreciated that his drawings must be in consideration of *agricultural* work on the holding. When diversification is undertaken, therefore, it is important to plan carefully and ensure that potential successors, such as the tenant's sons, are engaged wholly in the agricultural part of the enterprise—even if the diversified nonagricultural business generates greater earnings.

The succession scheme also provides that, to be eligible, a successor must not be occupying a "commercial unit of agricultural land" at the time of the tenant's death or retirement.<sup>44</sup> The principle underlying this rule is to prevent succession taking place where the applicant, for example the farmer's son, already owns or rents a holding substantial enough to provide a reasonable income. Careful planning will again be required to ensure that a potential applicant avoids this pitfall. Curiously, however, this provision, unlike the livelihood condition, works to the tenant's advantage when diversification into nonagricultural farm business takes place. Whether land occupied by the applicant constitutes a "commercial unit," disqualifying him from succeeding to the tenancy, is determined in accordance with Schedule 6, paragraph three of the 1986 Act. This specifies that a commercial unit of agricultural land means "a unit of agricultural land which is capable, *when farmed under competent management*, of producing a net annual income of an amount not less than the aggregate of the average annual earnings of two full time, male, agricultural workers aged 20 or over" (*italics added*).<sup>45</sup> A successful nonagricultural business, such as a retail farm shop, may generate considerably more income on a small portion of the holding than can be achieved by traditional farming. For succession purposes, however, that land will be assessed not on the income it actually produces, which may be considerable, but on the income it would produce if farmed properly—a very different proposition. The farmer's son may own or rent a small holding which is fully diversified and very profitable. He will only fall foul of the commercial unit test if the acreage of the holding is such that it would, if farmed appropriately, generate enough income for two farmworkers.

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41. An applicant also may show agriculture is his principal source of income with two or more discontinuous periods together amounting to not less than five years total. The applicant will be treated as dependent on farm income during periods (up to a maximum of three years) when he is attending full time education courses at a university or college. *Id.* at sched. 6, para. 1.

42. See generally *Trinity College Cambridge v. Caines*, 272 E.G. 1287 (1983).

43. See *Welby v. Casswell*, 35 E.G. 126 (1994).

44. Agricultural Holdings Act, 1986, § 36(3)(b) (Eng.).

45. *Id.* at sched. 6, para. 3.

### E. Implications for Rent Review

Diversification will also have implications for the level of rent payable under an agricultural tenancy, although the issue was not, until recently, free of doubt. Where the rent has to be settled by arbitration, the arbitrator is directed by the 1986 Act to calculate the rent at which the holding might reasonably be expected to be let by a prudent and willing landlord to a prudent and willing tenant. In assessing this he is enjoined, further, to have regard to "all relevant circumstances," including the character and situation of the holding, the terms of the tenancy, the "productive capacity" and "related earning capacity" of the holding.<sup>46</sup> The rent formula seeks, albeit imperfectly, to tie the rent payable to the productive potential of the holding. Both productive capacity and related earning capacity are defined in strictly agricultural terms. Productive capacity, for example, means the productive capacity of the holding, with the fixed equipment provided, on the assumption that it is in the occupation of a competent tenant practicing a system of farming suitable for the holding.<sup>47</sup>

If the tenant diversifies, will any additional income generated be accountable on rent review? It is clearly not attributable to "productive capacity" or "related earning capacity" in the sense previously mentioned. It was held, nevertheless, in *Enfield London Borough Council v. Pott*,<sup>48</sup> that income from a farm shop could be taken into account as a "relevant factor" under the general clause in the rent formula. Some weight is added to this county court judgment by the Court of Appeal's ruling in *Trustees of J. Childers v. Anker*<sup>49</sup> where it was held that nonagricultural income from an environmental management agreement was, likewise, a "relevant factor" which could be taken into account on rent review. Compensation paid under the management agreement for the restrictions it placed on the agricultural operations which could be carried out by the tenant was the "equivalent" of actual earning capacity, in that it was replacing it, and should therefore be relevant for the purposes of the rent formula (per Morritt LJ.).

If the tenant makes improvements as part of a diversification scheme, any additional rental value thus generated will be disregarded. In *Tummon v. Barclays Bank Ltd.*,<sup>50</sup> it was held that tenant improvements of both an agricultural and nonagricultural nature must be disregarded,<sup>51</sup> with the result that a caravan park created on the holding was treated as a tenant's improvement to be disregarded for rent purposes.<sup>52</sup> The statutory disregard for tenant's improvements does not extend to business goodwill, however, and this *may* be accountable on review.

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46. *Id.* at sched. 2, para. 1.

47. *Id.* at sched. 2, para. 1(2).

48. *Enfield London Borough Council v. Pott*, 34 E.G. 60 (1990).

49. *Trustees of J. Childers v. Anker*, 1 E.G.L.R. 1 (1996).

50. *Tummon v. Barclays Bank Ltd.*, 39 P. & C.R. 300 (1979).

51. *Id.* at 312.

52. *Id.* at 309.

### F. Compensation on Termination of Tenancy

One final problem concerns compensation for improvements to the farm made by the tenant. If the farmer has successfully diversified, he may have made considerable improvements to the holding which increase its rental value in the landlord's hands. A tenant's improvements will be disregarded on rent review. The tenant, however, will not be able to claim compensation at the end of the tenancy for nonagricultural improvements. This follows from Schedule 7 of the 1986 Act, which lists those improvements for which compensation will be available.<sup>53</sup> Improvements which are chiefly agricultural in nature, such as the erection of silos and fencing are compensatable. Some nonagricultural improvements, such as the heading of "erection, alteration, or enlargement of buildings," or the making of roads and bridges, may qualify for compensation under the Act. Even if the improvements qualify for compensation, the measure of compensation is fixed by section sixty-six by reference to the amount by which they enhance the letting value of the holding *as a holding*.<sup>54</sup> This may bear no relation to the true increase in letting value of the farm consequent upon a successful diversification.

### III. FARM BUSINESS TENANCIES: A NEW FRAMEWORK

The Agricultural Tenancies Act 1995, which came into force on September 1, 1995, introduced a new legal framework for farm tenancies granted on or after that date. The new legislation offers a completely new approach to land tenure, and is based firmly on principles of freedom of contract. The 1995 Act introduces greater flexibility into arrangements for land tenure and the management of tenanted farms and removes most of the restrictions applicable to tenancies under the 1986 Act. Its primary objective is to encourage a revival in the tenanted sector by removing the existing disincentives to lease land—principally the extensive security of tenure enjoyed by tenants under the 1986 Act. It also seeks to provide a more suitable legal framework for encouraging the diversification of farm businesses and reflects the current concern with promoting a more widely based rural economy. Tenancies under the 1995 Act will be known as "Farm Business Tenancies."

The 1995 Act provides two avenues to a Farm Business Tenancy. It is a condition of both, and of the creation of any farm business tenancy, that some, whether all or part, of the holding must be farmed in the course of a trade or business.<sup>55</sup> A farm business tenancy can be created where both the landlord and tenant give a written notice (to each other) at the time of the grant, stating that the tenancy is to be a farm business tenancy and that it is to remain such even if its character ceases to be wholly agricultural. This mechanism is intended to ensure that a tenancy will not cease to be within the Act if diversification takes place during the course of the tenancy, even if the extent of the nonagricultural use effectively changes the character of the ten-

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53. Agricultural Holdings Act, 1986, sched. 7 (Eng.).

54. *Id.* § 66.

55. Agricultural Tenancies Act, 1995, § 1(2) (Eng.).

ancy. Alternatively, where the notice provisions are not used, a tenancy can still be a farm business tenancy, but only if the character of the tenancy is "wholly or primarily" agricultural.<sup>56</sup> This requirement, the "agriculture condition," is assessed by examining the terms of the tenancy, such as inquiring whether the tenancy prohibits nonagricultural use. Further, examining the use of the land comprised in the tenancy, the nature of any commercial activities carried out on that land, and "any other relevant circumstances" provides an assessment of the agriculture condition. The agriculture condition must be met both at the time of the grant and at the time when any issue as to the holding's legal status arises. The tenancy can, in other words, move in and out of the 1995 Act as the use of the land changes.

The notice facility, in particular, is intended to encourage farm diversification, while avoiding the sort of legal pitfalls encountered by tenants under the 1986 Act as outlined above. If notice is given that it is to be a farm business tenancy, then even if the substantial use ceases to be agricultural, the tenancy will still qualify as a farm business tenancy providing that *some* of the land continues to be farmed in the course of a trade or business, the "business condition." The Act does not specify *how much* land must continue to be farmed, but, clearly, a tenancy which has ceased to be agricultural in substance could still qualify as a farm business tenancy under this provision. This will remove the problem encountered in cases like *Short v. Greeves*<sup>57</sup> under the 1986 Act, in which the issue is whether the "substantial" use had ceased to be agricultural. In the case of tenancies covered by the 1995 Act, the use can cease to be substantially agricultural without the status of the tenancy being affected, provided that the notice facility is used at the commencement of the tenancy.

This will encourage diversification without the complex legal issues which apply to holdings still governed by the 1986 Act. A few problems remain, however. For the notice procedure to be available, the character of the tenancy must be primarily or wholly agricultural at the beginning of the tenancy, with regard to the terms of the tenancy and any other relevant circumstances. If the letting is of land and premises, which are used from the outset for mixed business and agricultural purposes, then it cannot be a farm business tenancy, even if the notices are served. Similarly, when a tenant has diversified successfully under a farm business tenancy and wishes to retire, the landowner may have difficulty reletting the holding on the same basis, as the use of the land in the hands of an incoming tenant may not be primarily agricultural. Another requirement is that the business condition be satisfied at the outset, and throughout the tenancy. For example, at least some of the land would need to be farmed in connection with a trade or business. If the letting is initially of land for grazing recreational ponies, for instance, this condition will not be met—even if the land is later farmed on a commercial basis. Great care will be needed in the service of the notices to bring the farm business tenancy regime into play and in the drafting of the tenancy agreement itself.

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56. *Id.* § 1(3).

57. *Short v. Greeves*, 1 E.G.L.R. 1 (C.A. 1988).

If the notice facility is not used, a farm business tenancy will only arise if the agriculture condition is satisfied at the commencement of the tenancy and while it remains so. In this case, therefore, diversification will raise the same problems as to abandonment of agricultural use and tenancy status as apply to tenancies covered by the 1986 Act. Strangely, however, the scope for diversification under this type of farm business tenancy may well be less than under a 1986 Act tenancy. By virtue of section 1(3) of the 1995 Act, the character of the tenancy must be *wholly or primarily* agricultural for the farm business tenancy regime to be applicable.<sup>58</sup> In cases like *Short v. Greeves* and *Wetherall v. Smith* under the 1986 Act, the issue was whether the "substantial" use had ceased to be agricultural. On similar facts under the 1995 Act, the courts will have less scope to apply a generous interpretation. The protection of the 1995 Act will cease to apply as soon as diversification results in the *primary* use of the land let ceasing to be agricultural. This will be much easier for a landlord to establish. If the tenancy ceases to be a Farm Business Tenancy within the 1995 Act, it will not automatically qualify for protection as a business tenancy under the Landlord and Tenant Act of 1954, Part II unless the court can infer a variation in the contract to let the premises for the new purpose, such as from acquiescence in the changed use with actual knowledge.<sup>59</sup> The tenant may lose the protection of one statutory code by unilateral abandonment without acquiring that of another. To mitigate this potential hardship, the 1995 Act contains a special provision for the case when the farm business lease expressly forbids nonagricultural use. By virtue of section 1(8), any use of land in breach of the terms of the tenancy or any commercial activities carried on in breach of the tenancy agreement, shall be disregarded in determining whether at any time the tenancy meets the agriculture or business conditions unless the landlord has consented to the change of use, or acquiesced in the breach of tenancy.<sup>60</sup> The moral here is that the tenancy agreement needs to be carefully drafted.

The legal regime applied to farm business tenancies makes special provision for diversification, and many of the legal problems which arise under the 1986 Act are specifically dealt with for farm business tenancies under the terms of the 1995 Act. The tenant's right to compensation for improvements at the end of the tenancy is widened, and is not restricted to improvements of an agricultural nature.<sup>61</sup> The measure of compensation payable is the resulting increase in the value of the holding "as land comprised in a tenancy," a formula which seeks to recognize the possibility of the land no longer having a solely agricultural use at the end of the tenancy.<sup>62</sup> The tenant will also be entitled to compensation for any increase in rental value attributable to planning permissions which the tenant has obtained for the holding. Compensation for development value arising from planning consents is not available under the 1986 Act. Initially, this might seem to be a considerable

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58. Agricultural Tenancies Act, 1995, § 1(3) (Eng.).

59. *Russell v. Booker*, 5 H.L.R. 10 (1982).

60. Agricultural Tenancies Act, 1995, § 1(8).

61. Agricultural Tenancies Act, 1995, § 15(1). See also Agricultural Holdings Act, 1986, § 66 and sched. 7 (Eng.).

62. Agricultural Tenancies Act, 1995, § 20 (Eng.).

benefit to the tenant considering diversification, who may need planning consent for nonagricultural development or change of use. Compensation is restricted, however, to those planning consents which would, if carried out, constitute an improvement on the holding. It will not be available for change of use consents when no physical improvements to the holding are in prospect. More importantly, compensation will only be available if the improvement is one to which the landlord has consented in writing, and if he has consented to the making of an application for planning permission. The tenant does not share in the development value generated by the planning consent, as the measure of compensation is the increase in rental value of the land "as land comprised in the tenancy." There could be potential for disputes if the diversification carried out is of little long-term benefit to the holding or an incoming tenant. Potential examples would include war games, paintball games, or motorcycle rallying.

The new provisions also appear generous at first sight in conferring a right to compensation for intangible "advantages," as this may cover a number of matters not previously compensated under the 1986 Act. What constitutes an "advantage" is left undefined, however, except to the extent that it must be attached to the holding and be distinguished from a planning permission or an improvement.<sup>63</sup> It would include dairy quota and similar rights attached to the holding, but it would presumably exclude compensation for livestock quotas and for some types of business goodwill. Goodwill normally attaches to the business, not the holding *per se*, and as such cannot be compensated for under the terms of the 1995 Act. This type of goodwill, which goes with the departing tenant, is frequently referred to as "dog" goodwill. In some cases, however, some goodwill *may* attach to the holding and remain after the tenant's departure (so-called "cat" goodwill). Examples would include the goodwill attached to a go-cart track established on the farm, an equestrian centre, a golf course, or a health club which will remain in business under the new occupant. These are all instances in which some residual goodwill may attach to the holding after the tenant's departure and this may now be compensated for the first time. Difficult questions will arise, however, in valuing goodwill and in distinguishing cat and dog goodwill in individual cases. The provisions for compensating intangible advantages will also allow for compensation for licenses acquired for the running of a diversified nonagricultural business, such as restaurant and liquor licenses for a farm cafe or restaurant or for a residential complex providing farm holidays. Valuing the measure of compensation for intangible advantages of this kind may also prove difficult.

The 1995 Act leaves the parties free to negotiate the length of the tenancy and offers no security of tenure to the tenant beyond the term agreed. This is, of course, a major departure from the approach favored by previous Agricultural Holdings legislation and to the security afforded to tenancies under the 1986 Act. Residual security is afforded the tenant in that if the lease is for a term of two years or more, it will continue as a tenancy from year-to-year on its expiry, unless notice to terminate the tenancy is given

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63. See *id.* § 15(b).

at least twelve months before its expiry date. A tenancy from year-to-year can, similarly, only be terminated by giving notice to quit of at least twelve, and not more than twenty-four, months duration ending on a term date of the tenancy.<sup>64</sup> There is no minimum term length and no statutory provision for security of tenure if a valid notice of termination is given, regardless of how long the tenancy has lasted. It should be noted, however, that there is no equivalent for the statutory forfeiture procedure offered by Case B to Schedule 3 of the 1986 Act, which applies where the landlord wishes to resume possession for his own nonagricultural use.<sup>65</sup> If the landlord has obtained planning permission for a nonagricultural development, the landlord will have to serve notice of termination of between twelve and twenty-four months duration. There is no special facility enabling him to serve short notice, as under the 1986 Act.

In matters of rent, the 1995 Act adopts an approach based on freedom of contract. The parties are free to agree to the initial rent for the letting without restriction and can provide for rent reviews under an agreed formula included in the tenancy agreement, itself. Alternatively, they can expressly provide that the rent shall be unchanged throughout the tenancy. The Act provides a fallback dispute procedure, allowing for arbitration on rent at three yearly intervals, but only when the tenancy does not include express provision for reviews or a fixed rent. In this event, the arbitrator is enjoined to establish a free market rent for the holding. In so doing, he must have regard to the terms of the tenancy and "all relevant factors."<sup>66</sup> Applying the rationale of the decisions on the rent formula in the 1986 Act, it is suggested that this would include income generated from diversified nonagricultural business activities on the holding.<sup>67</sup>

#### IV. CONCLUSION

Clearly, the 1995 Act provides a legal framework more appropriate to the economic realities of farming in the 1990s than the regime of the Agricultural Holdings Acts. Will the 1995 Act, in practice, provide a legal medium which encourages greater diversification? Two conditions are necessary, it is suggested, for successful diversification: (1) a legal framework of rights which allows for nonagricultural use within the confines of the farm tenancy, and confers appropriate rights and duties on the parties where nonagricultural diversification is envisaged, and (2) long-term security will be necessary to successfully plan and execute a diversification scheme. Diversification is a long-term business option, and cannot be executed overnight. It will require detailed investment and finance planning. It may be necessary to prepare and to make planning applications for building work or change of use. Of course, no farmer is going to make considerable financial inputs without long-term

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64. Sections 5 and 6 of the Act set out the notice provisions applicable to farm business tenancies.

65. Agricultural Holdings Act, 1986, sched. 3 (Eng.).

66. See Agricultural Tenancies Act, 1995, § 13(2).

67. See *Enfield LBC v. Pott* 34 E.G. 60 (1990); *Trustees of JW Childers v. Anker*, 1 E.G.L.R. 1 (1996).

security to realize his investment, and he needs a suitable legal regime guaranteeing compensation for any enhancement in the value of the holding which results.

The Agricultural Holdings Act gives tenant farmers long-term security, but, as we have seen, it provides a legal framework wholly unsuitable for the diversified farm enterprise. The Farm Business Tenancy, on the other hand, provides a legal framework more suited to the diversified enterprise. Arguably, however, it does not give the farmer sufficient long-term security within which business plans for successful diversification can be brought to fruition.

The 1995 Act prescribes no minimum term for farm business tenancies, and given complete freedom of contract, many landowners will grant short-term tenancies which offer little long-term security. This basic weakness in the farm business tenancy concept, from the tenant's standpoint, may prove vital to its possible impact on the prospects for diversification. Some landowners will, doubtless, grant long fixed term tenancies within which diversification can be planned and executed. In this type of case, the new legislation provides a much improved regime for encouraging diversification. It should be appreciated that even here, however, the tenant has little scope for independent action. The landowner's consent will be needed for improvements and planning applications if compensation for improvements is to be available at the end of the tenancy. This is appropriate, if the character of the land let will be changed as a consequence of the diversification proposed. The landlord will, after all, be getting back a holding substantially different in character to that originally let. It does mean, however, that the tenant under a farm business lease will in practice enjoy little more freedom of action than his counterpart under a 1986 Act tenancy. One suspects that long-term tenancies are unlikely to be the norm, and if this proves to be the case the 1995 Act may have less impact than its proponents have predicted.

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