

**IMPACT OF AGRARIAN REFORM  
ON LANDOWNERS:  
A REVIEW OF LITERATURE  
AND A CONCEPTUAL FRAMEWORK**

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# **IMPACT OF AGRARIAN REFORM ON LANDOWNERS A REVIEW OF LITERATURE AND A CONCEPTUAL FRAMEWORK**

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## **I INTRODUCTION**

The 1987 Constitution provides that "the state shall promote comprehensive rural development and agrarian reform." It requires the state to provide incentives to landowners to encourage them to invest the proceeds of the compensation for their lands under agrarian reform to promote industrialization, employment creation, and privatization of public sector enterprises. It provides that financial instruments used as payments for lands shall be honored as equity in public enterprises where landowners chose to invest. These constitutional provisions are a major feature of the Comprehensive Agrarian Reform Program (CARP) signed into law (Republic Act 6657) by President Corazon C. Aquino on 10 June 1988.

Philippine studies on agrarian reform have dealt largely with the agrarian reform beneficiaries and the reform's effects on their welfare and production efficiency. Very little work has been undertaken on the agrarian reform's other major actor, the landowner. This is rather surprising in view of the important role expected of landowners in promoting industrialization and employment.

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This paper presents a review of literature and related experiences on the impact of agrarian reform on the landowners, for two main reasons: (1) landowners are a legitimate concern of the government, and (2) policymakers and even social scientists view landowners as potential investors, entrepreneurs, and industrialists. The usual expectation is that landowners will assume another role, that of investors and entrepreneurs, once displaced from their land and given government incentives for them to join industry. It is interesting and significant to find out to what extent the expectation is realized, and if the contrary happens, to determine why.

Using secondary information and current literature, this paper documents and analyzes (a) the utilization of landowner's compensation under Presidential Decree 27 and RA 6657, the laws that implement agrarian reform under the Marcos and the Aquino administration, respectively; (b) the factors that encourage or discourage the shift of landowners from agriculture to industry; (c) the existing incentives and support infrastructure given to them; (d) the impact of agrarian reform on their income and investment behavior; and (e) the current compensation program for them.

The paper is organized into five sections. Section I is the introduction. Section II looks briefly at the agrarian reform experience of Taiwan, Japan, and South Korea. Section III relates the Philippine experience in handling the landowners. Section IV proposes a conceptual framework for undertaking a study of the outstanding agrarian reform issues identified in the course of the review. The last section discusses the relevant issues and research priorities.

## **II. EXPERIENCE OF OTHER COUNTRIES**

This section looks briefly at the impact of agrarian reform on landowners in Taiwan, Japan, and South Korea. Special attention is given to the compensation schemes adopted by these countries. Table 1 presents a broad comparison of their agrarian reform profile, particularly the mode of compensation to landowners. In the three countries, the landlords were compensated in terms of bonds. In Japan, what appeared to be a reasonable price when first fixed was later eroded by inflation, virtually resulting in a confiscation of the landowners' land.

To avoid this, Taiwan tied the price of the land to payments in two principal products of the land and to shares of stocks in government-owned industrial enterprises. This method worked well for all parties concerned. The commodity bonds preserved the value of the sales price against fluctuations in the value of the currency for a ten-year period, while the government was freed from resorting to printing of money. The tenants also benefited from easy repayment terms.

In South Korea, no cash payment was involved. Landowners were simply paid in terms of commodity bonds, redeemable in any one year to only 30 percent of the crop's value.

How to pay for the land is a question of paramount importance for the government, landlord, and tenant. No matter what the price, the experience in East Asia showed that the

Table 1  
COMPARATIVE AGRARIAN REFORM PROFILE, ACCOMPLISHMENTS AND MODES OF COMPENSATION

Profile/Country	Japan	Taiwan	South Korea
I. Land Reform Law	1946	1953	1948, 1950
II. Time Period	1946-49	1949-53	1948-58
III. Area Covered			
000 Hectares	2,000	235	577
% of Cultivated Area	40.2	26.9	27.9
IV. Mode of Compensation	<p>Landowners were paid in bonds with interest rate of 3.66 percent, unredeemable for two years; principal and interest to be refunded in annual installments within 22 years. However, as the minimum face value of the bond was 1,000 yen, land priced at less than 1,000 yen was paid for in cash.</p>	<p>No cash payment. Landlords were paid 30 percent in stock shares of government enterprises and 70 percent in land bonds redeemable in kind.</p> <p>Bonds in kind were of two kinds: rice and sweet potato. Rice bonds were redeemable in rice upon maturity and sweet potato bonds redeemable in cash calculated in terms of the prevailing market price of sweet potatoes at the time of redemption. The bonds bore an annual interest rate of four percent and were redeemable in 20 semi-annual installments spread over a period of ten years.</p>	<p>Payment in bonds limited in redemption in any one year to 30 percent of the value of the crop estimated as an average harvest. The landowner was allowed this 30 percent of crops over a five-year period.</p>

Sources: Ghonemy, 1970; Kajita, 1959; King, 1977; Chao, 1972; Hayami, Quisumbing and Adriano, 1990

governments concerned did not choose to pay cash in one lump sum, but devised more manageable fiscal schemes.

#### A. *Taiwan*<sup>1</sup>

The land reform program in Taiwan was carefully carried out in the late forties and early fifties. It was instrumental in bringing about significant changes in industrial development. Before the reform, industrial production had little attraction for investment capital because of exorbitant land rents, mostly 50 percent of the total annual yield of principal crops. With huge profits obtained from the land, landlords were hardly interested to invest their capital in industry.

In 1949, Taiwan initiated land reform by reducing farm rent to a maximum 37.5 percent of the total annual yield of the main crop. This policy gave immediate relief to the tenant farmers. It raised their social status and appreciably brought down the price of farm lands, making it possible for them to buy land and become landowners. In turn, it lessened the incentives for landowners to withhold land, paving the way for the transfer of land to the tillers.

Having laid the solid foundation for land reform with the successful implementation of farm rent reduction, Taiwan proceeded to sell public lands by installment to enable more tenant farmers to become owner-operators and to set an example for the landlords, who were later required to sell their lands to the tenants.

The last phase of the reform was the implementation of the land-to-the-tiller program. It involved the compulsory purchase by the government of the landlord's tenanted farm lands in excess of a certain maximum limit, and the resale of such lands at the same price to the incumbent tillers.

The price of farm lands compulsorily purchased from landlords was 2.5 times the amount of the total annual main crop yield. The landlords were paid 30 percent in stock shares of four government enterprises and 70 percent in land bonds redeemable in kind.

The use of the stock shares of public enterprises as payment was aimed at privatizing those enterprises and at encouraging the landowners to invest their money in industry rather than in lands, as they had done so for centuries. It was also meant to finance the land transactions at the initial stage (Chao 1972).

The land bonds in kind were of two types: rice and sweet potato. Rice bonds were redeemable in rice upon maturity, and sweet potato bonds were redeemable in cash calculated in terms of the prevailing market price of the commodity at the time of redemption. All land bonds bore an annual interest rate of four percent and were redeemable in 20 semi-annual installments spread over a period of 10 years. These two methods of payment were designed

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1. This section of the review draws heavily from Shen (1966) and Koo (n.d.).

to take the place of money payments to avoid any inflation caused by a sudden increase in the amount of currency in circulation.

The interest of landowners was protected by a reasonable formulation of land transfer prices (2.5 times the value of annual crop yields) and payments procedures. The land bonds, aside from bearing reasonable interest rate, protected the holders from possible currency depreciation.

To ensure full eventual compensation to landlords holding land bonds, the Redemption Guarantee Fund was established in the Taiwan Land Bank. The Fund was drawn to pay landowners who were trying to redeem land bonds in case of delay or default in the installment payments by land purchasers. Also, while the landowners were paid in part with stocks of government enterprises, they were free to liquidate their holdings at any later date.

Apparently, these features of compensation gave landowners enough protection and were acceptable to them.

The farm lands compulsorily purchased from the landlords were resold by the government to incumbent tillers at the same purchase price. Paddy lands were paid for in rice bonds, except in some special areas where cash was more acceptable as a substitute for rice. Dry lands were paid for in cash, equivalent to the prevailing local market price of sweet potatoes. The farmer-purchaser was required to pay the land price, plus interest of four percent per annum in 20 semi-annual installments spread over a period of 10 years. But the total amount any given farmer had to pay in a year, including both the semi-annual installments and the land tax payable in his capacity as new landowner, did not exceed the annual farm rent he used to pay as tenant.

Land reform played a major role in hastening Taiwan's industrialization. Its most fundamental result was the change in the structure of the social economy. Limitations on the size of land that the landlords could own and on the purchase of farm land by noncultivating landlords changed the direction of private capital flow. The transfer of the four government enterprises to private hands not only absorbed the capital formerly frozen in land but also paved the way for the development of private enterprises. Stronger rural purchasing power and increased farmers' savings enhanced domestic capital formation, increased industrial investment, and pushed forward industrial development.

The Taiwan experience shows that agriculture and industry develop not to the mutual exclusion of each other. On the contrary, one cannot fully develop without the other. If land rent becomes a protected tool for generating fat and easy profit for a certain class within the economy, industrial development suffers. Taiwan's land reform removed this irrational mode of productivity and the tenancy system, thus eliminating the obstacle to industrial development (Koo n.d.).

## B. *Japan*

Land reform in Japan began in 1946 and was completed in 1950. Farmland holdings were compulsorily purchased by prefectural governments on behalf of the State, except for those pieces reserved for the owners. Land retention limit was set at 12 cho (1 cho = 0.99174 ha) in Hokkaido and an average of three cho in the rest of Japan (Dore 1959). The lands purchased by the government were then sold to tenant farmers.

Transfer prices of land were originally computed based on capitalized earnings in 1945 at the prevailing interest rate. These prices were pegged throughout the four-year period of land reform. Landlords were paid in bonds at 3.66 percent annual interest rate, unredeemable for two years, and principal and interest to be refunded in annual installments within 22 years. However, as the minimum face value of the bond was 1,000 yen, land priced at less than that amount was paid for in cash (Kajita 1959).

The government sold the land to tenant farmers at the same price paid to landowners. Since there was considerable inflation during that period, the pricing system proved to be very disadvantageous for the landowners. By the time they received the full payments for their land from the tenants, the sum was exceedingly small in real terms compared with the actual yields of the lands<sup>2</sup> (by 1950 the price of rice was more than 40 times that in 1945, when land values were calculated). The tenant farmers practically received land at a minimal cost due to currency depreciation.

Most landowners appealed to the government to revise the standard of land prices but were rejected. Land prices were not revised until the establishment of the owner-farmer system was completed in 1950. The landowners even appealed to the courts, but after a long dispute the Supreme Court ruled in December 1953 in favor of the government. This decision also officially recognized land reform as constitutional (Kajita 1959).<sup>3</sup>

Payments by tenants for the land were in cash or on installment basis over 30 years, at an annual interest rate of 3.2 percent. Since the total payments were such a small percentage of the annual yields, most tenants were able to pay within a year or two after purchase (Chao 1972).

As a result, about 80 percent of total tenanted lands was successfully distributed. The recipient households accounted for 70 to 80 percent of the total farm households then in existence. Since only resident landowners were allowed to retain land within the limits set by the government, absentee landowners had to sell their land. Thus, tenancy rate was reduced to

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2. Ceiling price for land and money rents were fixed. Also, there were severe restrictions against tenant eviction.

3. Japan did not create anything special (e.g., incentives) for landowners. Apparently, the landowners gave up their land (the land reform approach was virtually confiscatory) because it was too discouraging to hold on to it.



less than 10 percent after the reform; most of the remaining tenant lands were cultivated by part-owner farmers (Chao 1972).

### C. *South Korea*

South Korea became the third East Asian country where American involvement after the war produced a moderately sweeping land reform. In contrast to Japan and Taiwan, South Korea's land reform was hardly successful because of the Korean War of 1950-53 which came after the reform.

The majority of Korean farmers were small tenants when the country was liberated from Japanese imperial rule. Tenants paid farm rent as high as 50 to 70 percent of their produce. This went to absentee landlords who made up a small but wealthy aristocracy (Pak 1956). Overconcentration of man-land ratio in farm villages caused farm rent to shoot up. Naturally, the Korean farmer hungered for land or at least wanted secure tenancy rights. The latter drove him to accept a position of personal subordination to landowners, giving rise to a class system in the farm society (Pak 1967).

When the US occupied South Korea in 1945, it immediately vested all Japanese-owned lands to the US military government, which conveyed these lands to the tenants. This represented the first stage of the Korean land reform. The procedure was simple, involving little financial burden since no compensation was paid to landowners. Tenants paid three times the standard production value of the land in 15-year installments at no interest. Rapid inflation virtually cancelled out these repayment obligations (King 1977).

The US military government also limited farm rents to a maximum of one-third of crop production and prohibited unilateral cancellation of tenancy contracts. Many landowners, foreseeing more thoroughgoing reform, sold their farmlands. Tenancy rate dropped, and the number of owner-farmers increased between 1945 and 1949.

In 1950, the Republic of Korea enacted land reform. The law established a retention limit of three hectares and declared most forms of tenancy illegal. However, by the time the reform was implemented, much of the land over three hectares had been sold or divided into smaller units. The farms were sold to tenant farmers at prices expressed in measures of grain, usually 150 percent of the total value of one year's crop. They were allowed to pay 30 percent of the crop for five years. The landlord was given bonds redeemable in any one year, but limited to 30 percent of the average value of the crop. He was allowed this 30 percent of the crop over a five-year period (Park 1956).

Compensation to landlords was so low, and was further eroded by inflation, that their investment in industry practically stopped. In fact, most dispossessed landlords promptly went bankrupt. The beneficiaries also experienced financial problems. Many of them, forced into debt to local moneylenders by lack of other adequate credit sources, mortgaged their land and thereby illegally renewed tenancy (King 1977).

The fragmentation of landholdings and the continued pressure on the land partly because of the influx of war-time refugees from the north, coupled with the official abolition of tenancy, led to disguised forms of tenancy arrangements which became all the more difficult to control. Disguised tenancy became prevalent particularly in densely populated rice-growing regions of the southwest. Under the system of semi-permanent contract farming, a laborer and his family agree to a given set of farm tasks, receiving from the landowner payment in kind, usually rice, prior to the crop season (Ledesma n.d.).

Early attacks on land tenure problems (even in the face of such considerable obstacle as the Korean War), lack of finance, and the breakdown of agricultural services had several positive effects. Centuries-old landlordism was destroyed. For the first time, the farmers enjoyed democracy and ownership rights. Land reform reduced the feeling of personal subordination and increased independence and individualism. In a way, the War made its contribution--landowners were unable to consolidate their opposition to land reform, and the farmers who persevered strengthened their claim to the land (King 1977).

### III. THE PHILIPPINE EXPERIENCE

#### A. *Payments to Landowners Under PD 27*

Compensation to landowners under PD 27 was made in either of these two ways: (1) the tenant-farmers pay the landowners directly in 15 equal amortizations yearly at six percent interest per annum, with the Land Bank of the Philippines (LBP) guaranteeing the payments; or (2) the LBP pays the landowner directly, then collects the 15 yearly amortization from the tenant-farmers.

Under the latter, the landowner can choose any of the following modes of payment: (a) cash payment of 10 percent of the total compensation, and the balance in 25-year tax-free LBP bonds with six percent annual interest; (b) payment of 30 percent in preferred shares of stocks issued by the LBP, and the balance in 25-year tax-free LBP bonds with six percent annual interest; (c) exchange arrangements for government stocks in government-owned or controlled corporations; and (d) such other modes of settlement as may be further adopted by the board of directors of LBP and approved by the President of the Philippines.

A 1976 survey of five regions (Montemayor and Tolentino 1977) showed that the majority (84 percent) of the landowners sampled chose to be paid through LBP. All of them wanted 10 percent in cash and 90 percent in LBP bonds. Of those compensated, 35 percent kept their bonds, and 25 percent sold their bonds and invested the proceeds, mostly in commercial activities.<sup>4</sup>

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4. Such investments included pawnshop, store, stock market, rural banking, and dealership in agricultural products and machineries.

The value of land transferred to beneficiaries was fixed at 2.5 times the average harvest of three normal crop years immediately preceding the promulgation of PD 27 in 1972. Such was also the compensation received by the landowner for his land. This formula has caused enormous administrative burden on the Department of Agrarian Reform, both in determining the yield and in resolving disputes arising from such determination. It was also a source of widespread dissatisfaction among landowners and of prolonged disputes between landowners and beneficiaries. It may be considered one of the most widely criticized aspects of Operation Land Transfer (World Bank 1977).

Other complaints about landowner compensation were: (a) the 25-year maturity period for the bonds was too long, especially with the delay in the processing of compensation papers; (b) the bonds have low market value; (c) the six percent annual interest on the bonds was too low compared with the high interest landowners pay on loans; (d) the 10 percent cash portion of the compensation was too small; (e) the bonds could not be used for tax arrears; and (f) only 80 percent of the face value of the bonds was good as collateral for loans (Montemayor and Tolentino 1977).

#### B. *Payments for Landowners Under RA 6657*

Under the Comprehensive Agrarian Reform Law (CARL), the landowner is compensated based on the cost of acquisition of the land, its current value, its nature, actual use and income, the sworn valuation, tax declaration, and the assessment made by government assessors.

This multifactor formula has caused some problems. Foremost was the lack of systematic and reliable data base, particularly on land sales, which make valuation initially difficult. Also, it gave room for manipulation of land sales data, which led to overvaluation of the land. Another problem was the rather complicated calculations (which an ordinary agrarian reform officer finds difficult) inherent in the formula (Cornista 1990).

The compensation is paid in one of the following modes, at the option of the landowner: (a) a portion in cash (depending on the size of the land) and the balance in government financial instruments negotiable at any time; (b) shares of stocks in government-owned or controlled corporations, LBP preferred shares, physical assets, or other qualified investments in accordance with the guidelines set by the Presidential Agrarian Reform Council (PARC); (c) tax credits which can be used against any tax liability; and (d) LBP bonds.

Market interest rates for LBP bonds are aligned with the 91-day Treasury Bill rates. Ten percent of the bonds' face value matures every year, from the date of issuance until the tenth year. The bonds can be used to purchase government assets to be privatized and as security for loans with any government and other financial institutions. However, former landowners do not seem to have enough incentives to try business ventures, apparently because these bonds do not have strong secondary market. Besides, the 10 percent of the bonds which matures every year is too small to use as capital.

Since the Aquino administration's agrarian reform program was implemented only in 1988, it is understandable that very few studies had been made on the landowner's utilization of the compensation from CARL. Cornista *et al.* (1989) made such a study, particularly of the utilization of compensation arising from the Voluntary Offer to Sell (VOS) scheme. At the time of the study, 30 landowners throughout the country have been fully or partially paid by the LBP under the VOS scheme.

The study was able to draw responses from 24 landowners. For the cash portion, 54 percent of the landowner-respondents used it to pay loans to the LBP and the Development Bank of the Philippines (DBP), to which the particular lands covered by the CARL have been mortgaged for some time prior to the VOS. As for the bonds, the landowners either allowed them to mature or converted them to cash at 96 percent of the face value. The majority (58 percent) kept their bonds to convert them to cash later, or to wait for payment of the matured portion and of the interest. The rest (42 percent) converted their bonds to cash for investment.

The study concluded that the actual utilization of the compensation (cash and bonds) indicated that the landowners lacked interest in promoting rural-based industries or in creating additional employment. Landowners who offered to sell small farms considered the proceeds from the LBP too meager to invest in a new and viable business. In fact, they considered the proceeds (regular payment and interest earnings) as substitute for the income they should have earned had the land not been subjected to VOS. On the other hand, landowners who sold large farms and opted to monetize their bonds preferred to invest in income generating ventures.<sup>5</sup> Nonpreference for rural-based industries may be due not only to the perceived high risk of such ventures but also to insufficient knowledge of the available opportunities open to rural enterprises. Further, government assistance to landowners on alternative investment opportunities was deemed inadequate.<sup>6</sup>

The Cornista *et al.* study draws the following issues:

1. Lack of incentives for landowners to invest the proceeds from agrarian reform to promote industrialization, generate employment, and facilitate the privatization of public sector enterprises;
2. Inadequacy of the cash portion to induce the landowner to engage in industry;

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5. Such as real estate development for housing, money lending, buy-and-sell, and RTW business.

6. The CARL provides that "the PARC, with the assistance of such other government agencies and instrumentalities as it may direct, shall provide landowners affected by the CARP and agrarian reform programs with the following services: (a) investment information, financial and counselling assistance; (b) facilities, programs and schemes for the conversion or exchange of bonds issued for payment of the lands acquired with stocks and bonds issued by the National Government, the Central Bank, and other government institutions and instrumentalities; (c) marketing of traditional and nontraditional financial markets and stock exchanges; and (d) other services designed to utilize productively the proceeds of the sale of such lands for rural industrialization."

3. Inadequacy of assistance given to landowners for alternative investment opportunities; and
4. Delays in the payment of compensation.

C. *Options for a Landowner*

The CARL has two basic schemes by which tenurial status can be changed: land acquisition and distribution, or nonland transfer program. Under the first scheme, the landowner can subject himself to any of the following modes: compulsory acquisition, VOS, or voluntary land transfer. Under the second scheme, the landowner, wherever applicable, can opt for any of the following: leasehold arrangement, production and profit sharing, and corporate stock distribution.

Under *compulsory acquisition*, the DAR identifies the land to be acquired as well as the beneficiaries. The landowner is notified about the DAR's decision to acquire the land together with an offer to pay. The landowner then informs the DAR of his acceptance of the offer. In case of rejection by the landowner, the DAR conducts administrative summary proceedings to determine compensation for the land. Interested parties are asked to submit evidence for just compensation. After submission, the DAR makes decision. Any party who disagrees with the decision may bring the matter to the court for determination of just compensation.

Under *voluntary land transfer*, landowners may enter into a voluntary arrangement with qualified beneficiaries for direct transfer of their land. Notices of land transfer must be submitted to the DAR within the first year of implementation of the CARP. This arrangement is duly recorded and monitored by DAR. The farmer-beneficiary may make direct payment to the landowner in cash or in kind under terms mutually agreed upon by both parties.

Under *VOS*, landowners may offer their land to the government. An additional five percent cash component is given as incentive. The remaining portion is paid in terms of the usual LBP bonds.

The *leasehold* arrangement involves the fixing of just rentals in tenanted lands within the landowner's retention area and in lands to be covered but not yet acquired under compulsory acquisition.

Under the *production and profit sharing* scheme, three percent of the gross sales is distributed to regular and other farmworkers if such sales exceed ₱5 million per annum. An additional 10 percent of the net profit after tax is also distributed to the farmworkers should the landowners realize profit. This scheme applies to individuals or entities owning or operating, under lease, agricultural lands pending final land transfer.

*Corporate stock distribution* is an option which may be availed of by corporate landowners in lieu of direct land transfer. Corporations owning agricultural lands may divert a portion of their capital stock equivalent to the value of the land assets devoted to agricultural

activities. The farmworkers become co-owners of the corporation instead of acquiring the land. However, such stock distribution plan must be approved by the PARC within two years from the effectivity of RA 6657, otherwise the land shall be subject to compulsory acquisition and subsequent distribution.

D. *Implications of the Options Available to Landowners*

The starting point for determining the amount of compensation is the landowner's declaration of "fair market value." Owners are also given the option to receive compensation directly through a voluntary agreement for direct land transfer to beneficiaries (RA 6657, Chap. VI, Sec. 21). Under the voluntary arrangement, however, landowners may coerce their tenants and farmworkers to arrive at an agreement favorable only to themselves. Even under the compulsory acquisition scheme, the DAR does not have the final say on the level of compensation. Landowners are allowed to contest in court DAR decisions and all related matters. By limiting the DAR's power of judicial review, CARL will almost certainly be stalled due to court cases.

Corporate landowners are also given concessions, such as a means to avoid land transfer through stock distribution. Qualified beneficiaries are allowed to purchase only "such proportion of the capital stock of the corporation that the agricultural land, actually devoted to agricultural activities, bears in relation to the company's total assets." Under this provision, the corporation can claim that its land assets represent a small portion of its total assets and, thus, it would offer to sell only that portion of the corporation's shares.

Further, the law provides that qualified beneficiaries are given only "the right to purchase" shares and will have no reduction in their compensation at the time the stocks are distributed. Given the low income of farmworkers, they would probably rather use their compensation for immediate consumption than pay for a (small) portion of the corporation's stock.

Still further, many landowning families can simply transfer the title of their land to established family corporations to evade actual land distribution. In effect, only the stock distribution option will be available to farmworkers.

In the case of VOS, a possible "manipulation" can take place. The landowner can offer to sell the worst possible land among his holdings and try to get the best deal out of it. This is reinforced by the retention limit of five hectares for himself and another three hectares for each of his children. Assuming an average of two heirs, this means an effective retention limit of 11 hectares. Certainly, landowners would choose the best lands for their retention. The effectively high retention limit will remove a substantial portion of cultivated land from agrarian reform coverage.

All these implications tell us that the loopholes in the agrarian reform program can enable the landowner to evade actual land transfer, which will impair the program's goal of land redistribution and industrialization.

#### IV. A CONCEPTUAL FRAMEWORK

The impact of agrarian reform on landowners is an important yet often neglected issue. It involves the questions of how they utilize the compensation they receive for their expropriated lands, their attitude toward becoming new entrepreneurs or investors, and what incentive structures and mechanisms induce their behavior.

As practiced in several countries, landowners are paid in government bonds, which in a sense forces them to invest in government-owned or -controlled industry or firms. Sometimes part of the compensation is made in cash. Possible outlets for this money include hoarding, luxury consumption, investment in city houses, urban land speculation, investment in industry, or investment in agricultural improvements.<sup>7</sup> The most important of these is probably investment in industry because of its effects on the long-term growth of the economy.

On the impact of agrarian reform on landowners and industry, the common notion is that the landlord's capital "tied up" in the land can be diverted to productive use in the form of increased investment in industry. Eddie (1971) argues that such a notion is a myth. He says that "existing real assets cannot magically be transformed into new assets of a different form. This is not to say there will be no diversion of landlord 'capital' from agriculture to industry, even in the short run. But it is likely to be working capital formerly supplied by landlords which is diverted, as well as some agricultural land which may be put to non-agricultural use, either to escape expropriation or because the land reform law has made the alternative use more profitable."

The method of financing compensation has a bearing on investment. Under the CARP, land acquisition and distribution are financed mainly from two sources: the Agrarian Reform Fund (ARF) and government budgetary appropriations. These sources are supposed to cover the difference between what is paid for the land<sup>8</sup> and the revenue received from its sale to beneficiaries.

The ARF consists of proceeds from the sale of government assets through the Assets Privatization Trust (APT) and from the ill-gotten wealth recovered by the Presidential Commission on Good Government (PCGG). Budgetary appropriations, on the other hand, can

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7. Faced with a reduced land area, the expropriated landowner may be forced to intensify cultivation of his retained land to maintain satisfactory income.

8. This includes not only price of the land but all the other costs involved in land transfer and acquisition, such as processing, titling, land surveys, etc.

be financed through either of the following: domestic borrowing, taxes, money creation, and foreign borrowing.

If landowners used the entire compensation for their land to buy new capital equipment or to invest in productive enterprises, and the compensation was financed by domestic borrowing, this only means that someone else's investible savings were transferred to the former landowners, who became the investing agents for these funds. In this case, no increase in net investments has occurred. However, there may be a change in the composition of investment as landowners turn away from agriculture. In this limited sense, landowners' "capital" is diverted away from agriculture to industry or trade; but again the new industrial investment comes not from capital "tied up" in land but from a net change in the savings behavior, in which the funds used to compensate the landowners were borrowed from the savings of private persons.

If the compensation is financed by a tax, both the consumption expenditures and the savings of those taxed would be reduced. If the landowners invest all the compensation, the proportion of investment out of a given level of income would indeed increase, but only because someone else's consumption was reduced. On the other hand, aggregate investment could decrease if the former landowners have a higher propensity to consume than those taxed to pay for the compensation.

Similarly, if the compensation is financed through money creation, and the landowners' expenditures led to employment of previously idle resources, this may lead to some increase in the economy's output, and some of the increase in real income may be invested or reinvested. But again, it is the change in income arising from this process, not the transfer of ownership of an existing asset, which led to an increase in the level of investment. Moreover, monetary expansion would almost inevitably bring inflation, leading to a willy-nilly transfer of the burden of compensation.

Foreign borrowing may be sought to finance land acquisition and distribution, although payments of compensation would almost certainly be made in domestic currency. The resulting foreign exchange inflow could be used either to expand domestic credits<sup>9</sup> or to increase imports. The servicing of foreign debt later could come from increased production as a result of higher levels of investment, which in turn could arise from credit expansion or increased imports.

Eddie, therefore, strongly argues that payment of compensation is merely an exchange of some financial assets for existing real assets. This has no immediate effect on the level of investment. The level and direction of real investment are affected by the redistribution of income and wealth, and by the induced changes in consumption and savings behavior of various groups who benefit from land redistribution.

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9. Note that inflation pressures may arise unless sterilized by monetary authorities.



In Taiwan, for example, the government encouraged landowners to develop the industry by converting their landholdings into industrial holdings. The only way investment, out of a given level of income, can be increased is to depress the aggregate average propensity to consume. The form of financing chosen will determine whether and how this would occur. It is the change in the use of income, not some process of unlocking capital tied to the land, that will increase net investment.

However, Eddie admits that the transfer of existing "capital" from agriculture to industry is possible when the landowners find it profitable to divert some of their land from agricultural to non-agricultural production. A likely transfer is the diversion to other areas of the working capital supplied by landlords.<sup>10</sup> The provision of credit by the LBP and the formation of cooperative organizations help in this diversion by providing alternative working capital other than that supplied by landlords.

The critical issues, therefore, are the incentives for landowners to shift from agriculture to industry and the mode of financing the compensation. If, inspite of the incentives, the landowners are not motivated to join industry, what are the causes or factors that hinder them? The starting point for analyzing them is the compensation package for landowners. Second is the institutions involved in assisting landowners to go into industry. Third is the macroeconomic environment that affects their behavior.

Figure 1 presents a framework for analyzing the impact of agrarian reform on landowners. Essentially, there are two major sectors involved: the agrarian sector and the industry sector.

As shown in the agrarian sector block, the reform program will change the land tenure system. Under the CARL, this is made operational either by land acquisition and distribution or by nonland transfer. In the former, the landowner is compensated for the expropriated land. Cash payment is not made in lump sum but is provided as an inverse function of farm size (Table 2). The balance is paid in LBP bonds maturing in equal annual installments over a 10-year period. Provisions are made for the transferability and negotiability of these bonds (Table 3). Early redemption is allowed, on condition that 30 percent of the proceeds should be invested in a company registered with the Board of Investments (BOI), or in the region where the landowner had previously made investments, subject to the guidelines that will be issued by LBP.

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10. Exchange relations continue to manifest themselves at the level of the production process. In this sense, one cannot simply view the pattern of exchange relations as separate from the sphere of production. For example, a landlord who lends to his tenant also enhances the feudal relations existing between them. It may be the case that the tenant, as a result of accumulated debts, is tied more to the landlord. Hence, the landlord is not only able to augment his output share by the interest he charges, but he is also able to assure the continuity of feudal relations. Under this situation, credit relation is symbiotic with other forms of surplus appropriation, such as land rent, merchant profit, etc. (Floro 1986).

**Figure 1**  
**Impact of Agrarian Reform on Landowners:**  
**A General Framework**

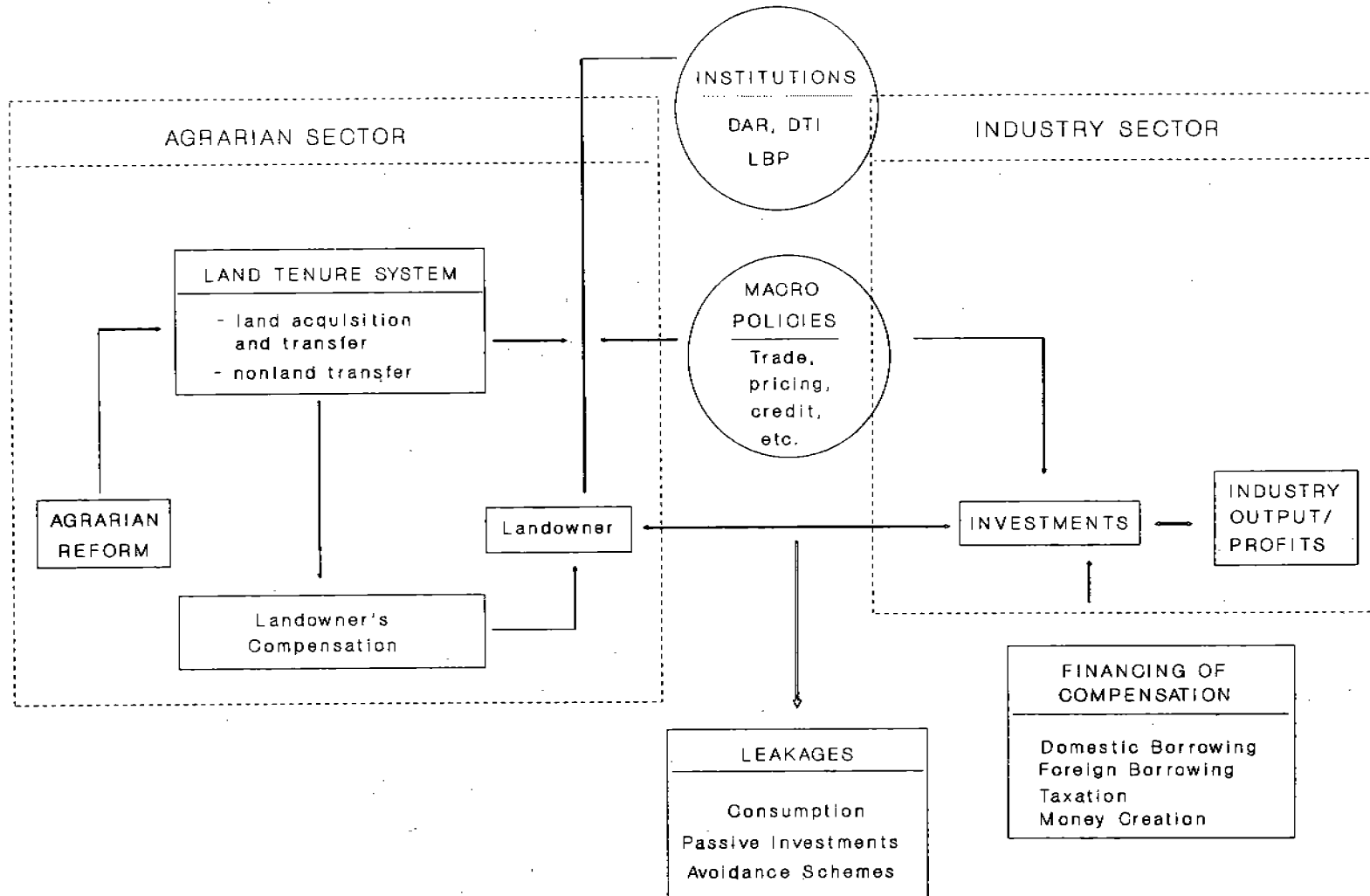


Table 2  
Modes of Payment to the Landowner Under RA 6657

- 
- Partial cash payment, and the balance in government financial instrument, under the following terms and condition:
    - 25 percent cash, balance in government instruments for lands above 50 hectares, insofar as the excess hectarage is concerned;
    - 30 percent cash, balance in government instruments for lands above 24 hectares and up to 50 hectares;
    - 35 percent cash, balance in government instruments for lands 24 hectares and below;
    - Additional five percent cash for lands voluntarily offered for sale.
  - In exchange of shares of stocks in government corporations.
  - As tax credits for any tax liability.
  - In Land Bank bonds.
  - Direct payment by the beneficiary to the landowner.
- 

Under the nonland transfer program, no actual land transfer takes place. The landowner stays in the land and arrangements are made to improve the tenurial status of the farmer. As pointed out earlier, the options under this program seem to be concessions to landowners.

The implementation of CARP produced expectation that, given his compensation and his displacement from the land, the affected landowner will shift to industry. However, the cash portion seems inadequate to induce the landowner to invest and engage in industry (Cornista *et al.* 1989).

To remedy this shortcoming, incentives are provided to landowners who invest in rural-based industries. These incentives are similar to those granted to a registered enterprise engaged in a pioneer or preferred area of investments as provided for in the 1987 Omnibus Incentives Code, or to such other incentives as the PARC, the LBP, or other government financial institutions may provide.

But even with the incentives, the landowner may not go into new investments for lack of technical know-how, fear of engaging in a totally unfamiliar business venture, and lack of

Table 3  
Features of the LBP Bonds Under RA 6657

- 
- bears market rates of interest aligned with 91-day treasury bill rates;
  - 10 percent of the face value of the bonds matures every year from the date of issuance until the tenth year;
  - transferable;
  - negotiable, up to the face value, for--
    - acquisition of land or other real properties of the government including assets under the APT;
    - acquisition of shares of stock of government-owned or -controlled corporations, or shares of stock owned by the government in private corporations;
    - substitution for surety or bail bonds;
    - security for loans with any government financial institution, provided the proceeds of the loans are invested in an economic enterprise, preferably in a small- and medium-scale industry, in the same province or region as the land for which the bonds are paid;
    - payment for taxes and fees to the government;
    - payment for tuition fees of the immediate family of the original bondholder in government universities, colleges, schools;
    - payment for fees of the immediate family of original bondholder in government hospitals.
- 

information on possible investment areas. Instead, the landowner may pursue activities that have lower risks and reasonable returns. This means the eventual transformation of the landowners to industrialists may not take place at all because of alternative options that are available to them. These options are referred to in the framework as "leakages," which may take the form of consumption, passive investment, or avoidance schemes.

Landowners may opt to use the proceeds of the compensation for consumption. This is more likely to be true for those who have small farms and whose proceeds from the LBP are

too meager to create a new viable business and are considered as substitute for the income they could have earned from the land.

Passive investments--such as placements in Treasury Bills, urban land speculation, city houses, etc.--are less risky options for landowners, yet they provide reasonable returns.

Perhaps the most significant form of leakage is the implicit avoidance option, or the agrarian reform program's loopholes, described in the previous section. Whether the loopholes are intended or not, the landowner can exploit them to evade actual land transfer. This is aggravated by the CARL's phased approach, where private agricultural lands are covered by the reform only in Phases II and III. This approach creates a state of uncertainty during transition, leading to (a) prior sale of land above the ceiling, (b) eviction of tenants due to anticipated reform at some future date, and (c) distribution of land among landowner's kin.<sup>11</sup>

Meanwhile, the bonds portion has limited negotiability since it can be used only for financial transactions with the government, such as acquisition of assets under the APT, and the like. Bond holdings of landowners should ideally earn returns equal to or above the net revenues they could have earned without the agrarian reform. However, there is no demand for the bond in the secondary market because of its limited features.<sup>12</sup>

The landowner can also be paid in terms of shares of stocks in government corporations. However, there is still a need to assess whether there have been substantial takers and whether the offers of these stocks, if any, have been attractive enough.

Other factors affecting landowners' investment decision are the existing macro-economic policies and the institutions that assist them in shifting to industry.

The behavior of landowners and the level of investments are affected by the existing macroeconomic environment. For example, if they decide to go into industry they would probably go to the protected industries for easy profits. Factors like trade, pricing, and credit policies affect the landowners' investment decisions. On the other hand, the absence of clear signals from the government, like a serious industrialization blueprint for the country, adversely affects the smooth and efficient transition from agrarian rent seeking to productive investments in industry.

Institutions also play a critical role in the whole process. The agencies basically involved in the acquisition and transfer of lands are the DAR and the LBP. The DAR notifies the

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11. It seems that the incentives structure and the political economy connive to make landowners retain the land and, thus, draw income from it as before. As a result, there is no shifting to industry by landowners. This is a hypothesis that deserves investigation.

12. Perhaps another reason for the absence of secondary market for the bond is that it is a nonbearer type and, therefore, has limited negotiability.

landowner of the offer to pay for the lands, which the landowner may accept or reject. If the offer is rejected, the DAR undertakes administrative proceedings. If accepted, the landowner submits to DAR all the required documents. The DAR reviews, evaluates and analyzes the landowner's claims folder (CF) to see if the data are complete.

Once found complete and accurate, DAR directs the LBP to pay the landowner. The LBP processes the CF and effects payment within 15 days. Figures 2 and 3 illustrate the activity flow for OLT and VOS programs. It should be noted that, in most cases, payments to landowners have been delayed (Montemayor and Tolentino 1977; Cornista *et al.* 1989), and the approval rate of CFs has been significantly low. The major reasons are the complex and tedious process of land valuation and the voluminous documentation requirements (Chan 1991). Recently, the land valuation function was transferred from DAR to LBP. The impact of this decision on land transfer and compensation process need to be assessed.

The LBP helps the landowners transform their bonds into liquid instruments by matching sellers and buyers of bonds. It also accommodates landowners who wish to avail of loans. The aim is to help landowners shift their capital from agriculture to industry and other productive enterprises.

The role of the Department of Trade and Industry (DTI) as defined by PARC is to provide management and entrepreneurship training to landowners to assist them in effectively channeling their resources to productive ventures. DTI also implements the Rural Industrialization Loan Fund (RILF) intended for CARP beneficiaries and displaced landowners who want to replicate prototype equipments established by the DTI. The RILF is used for relending and uses private voluntary organizations (PVOs) or nongovernment organizations (NGOs) as conduits. The prototype equipments financed by RILF are mainly designed for countryside industrial activity and are acquired at the provincial level by the DTI.

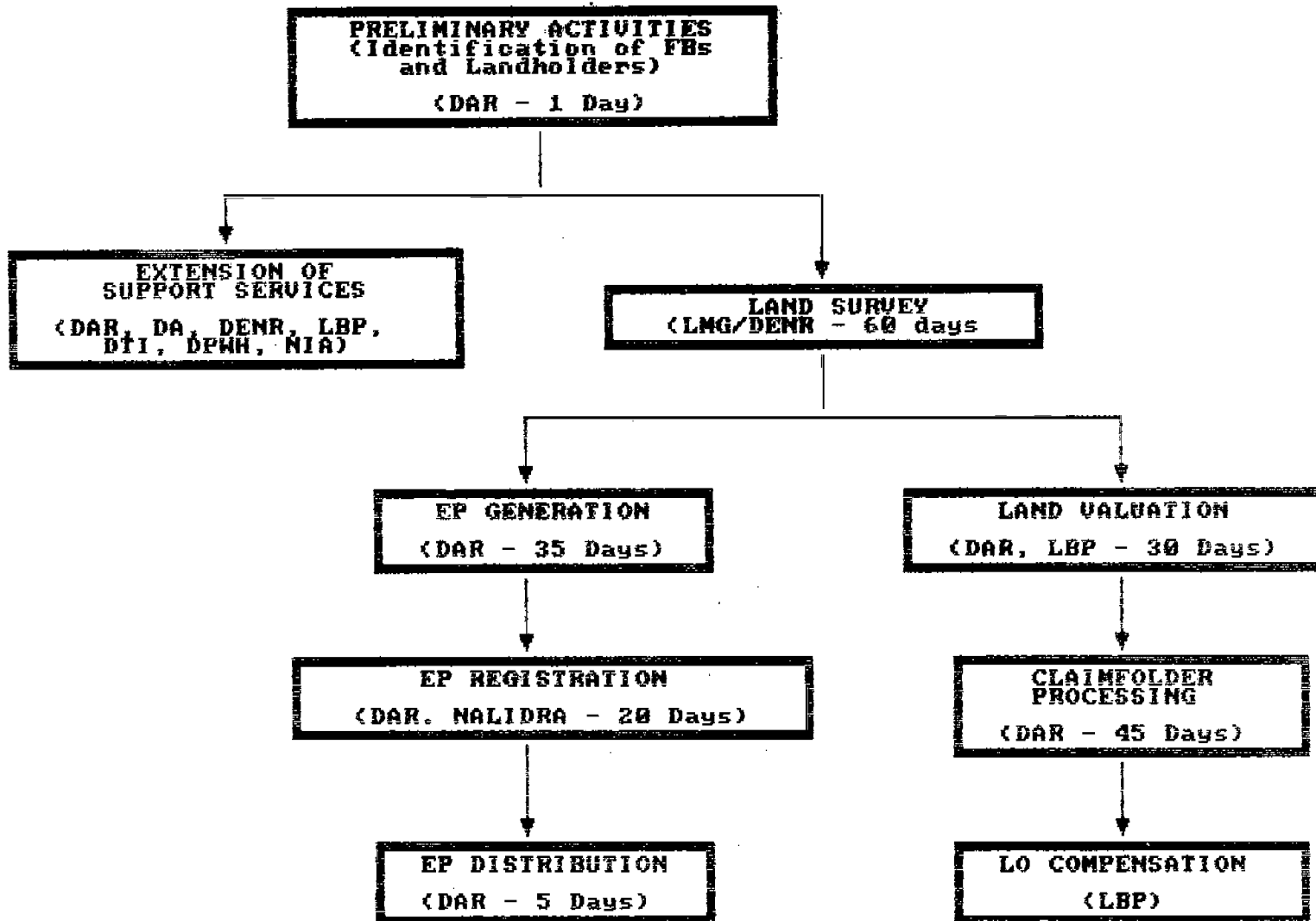
In the industry sector block of Figure 1, we see that the influence of factors affecting landowners' behavior has some impact on the level of investments, which in turn affects overall industry output. If profits are reasonable enough, then investments could rise and probably cause the landowner to increase his capitalization.

## **V. ISSUES AND RESEARCH GAPS**

In this review, we have looked into the compensation package of landowners and their utilization of such compensation in the Philippines and in other countries. The review concentrated on these areas because of the very few studies done on other factors that affect landowner behavior. As indicated in our objectives, our interest also covers the factors that motivate or discourage the shifting of the landowner from agriculture to industry, the existing incentives and support infrastructure to landowners, and the impact of agrarian reform on their income and investment behavior. While current literature has not touched on these, we have nevertheless analyzed and integrated them in our conceptual framework.

Figure 2

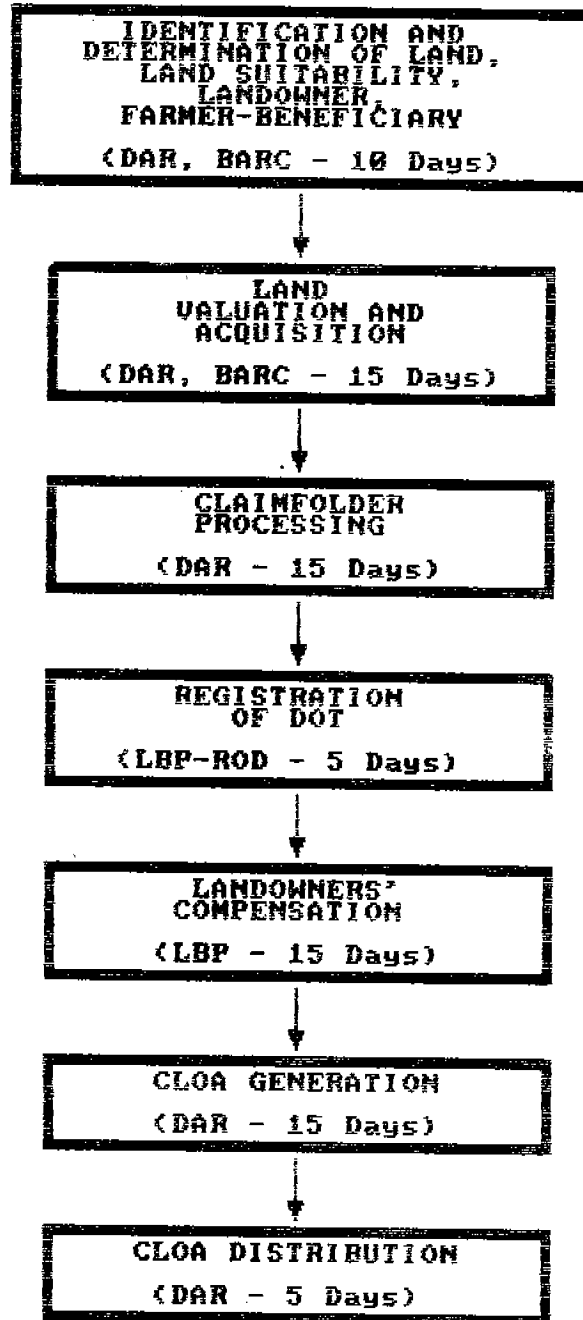
## OLT FLOW OF ACTIVITIES



Source: PARC

Figure 3

## VOS FLOW OF ACTIVITIES



Source: PARC



We have raised a number of issues that provide a basis for formulating a set of macro and micro research priorities. These issues point to some research gaps in agrarian reform, particularly on landowners.

On the macro concerns, three major issues are identified. First, the impact of the existing macro environment on the landowner and on investments. As we have said, the behavior of landowner will not only depend on the payment issued to him but, to a large extent, also on the existing macro environment, which includes trade, pricing and credit policies, the existing incentives structure, and infrastructure and support services. The critical issues are whether the existing policy framework sufficiently motivates the landowner to go into industry, and whether it has really spurred investments.

Second is the role institutions play in transforming landowners into a new class of entrepreneurs or investors. Given the magnitude of the task in terms of numbers and geographical dispersion, institutions responsible for implementing agrarian reform program play a very important role. To be effective, the program must have an appropriate institutional structure, as well as incentive schemes that will induce the desired objectives. The institutions involved must be enforcers and transmitters of incentives and effective motivators. The incentive system, on the other hand, must induce appropriate behavior from both the institutions and landowners. These things need to be closely looked into.

Third is the financing and mode of compensation. The bond portion of the compensation has limited negotiability. Therefore, it is important to look into how a strong secondary market can be developed for the bonds. Corollary to this is the convertibility of the bonds into shares of stock in government corporations, or their use to acquire government shares of stock in private corporations. Here we ask: What has been the response of the landowner to this offer? Has the government efforts in privatization able to attract the landowners affected by land reform? If not, what are the hindering factors?

At the micro level, a specific area for research is the utilization of landowners' compensation under different land acquisition schemes. This would give policymakers an idea of the extent of "leakage" involved in the system. Once this leakage is quantified and identified, possible measures can be considered and even instituted to insulate the system from such leakage. A closely related area is the documentation of the avoidance schemes taken by landowners. This is absolutely necessary because this would instruct policymakers about the loopholes of the agrarian reform program.

Another concern is the impact of agrarian reform on the income of the landowner. It would be interesting to see to what extent and to which direction has the landowner's income changed, and to determine what his investment decision has been as a result of such change.

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