

# MAKING AGRICULTURAL LAND MORE BANKABLE AND TRADEABLE



**COALITIONS** for **CHANGE**

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NEW LAW LIFTS RESTRICTIONS ON MILLIONS OF TITLES TO IMPROVE PRODUCTIVITY AND INCOMES IN PHILIPPINE AGRICULTURE

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In February 2019 President Rodrigo Duterte signed into law the Agricultural Free Patent Reform Act. Despite the lack of attention, the law has the potential to have an enormous impact on Philippine agriculture and for Filipino farmers because it removed two restrictions on 2.6 million parcels or 10 percent of all titled parcels in the Philippines. These two restrictions have discouraged commercial and rural banks from extending loans to holders of these titles and have hindered investments in technology and management systems that can increase the productivity and income of farmers. These restrictions are part of the reasons why agriculture has been the worst-performing sector of the economy, with an average annual growth rate of only 1.1 percent for the last decade.

This paper elaborates on how this important law was introduced. It begins with a brief overview of poverty and agriculture in the Philippines and the role of property rights in that nexus. It goes on to explain the restrictions, and its origins in the Public Land Act issued in 1936 and traces a four-year effort among various local leaders and organizations to update the policy framework to make land titles more bankable and tradeable to foster investment, employment, and growth. The main protagonists are Philippine leaders and the Foundation for Economic Freedom (FEF), a public advocacy organization working on reforms related to economic growth and good governance, and with support from *Coalitions for Change*, a program of the Australian Government and The Asia Foundation Partnership in the Philippines. The paper concludes with a set of lessons drawn from the reform experience.

*Coalitions for Change (CfC) is a program of the Australian Government and The Asia Foundation Partnership in the Philippines. CfC strategically supports the development, introduction, adoption, and implementation of key policies consistent with the government's agenda on economic growth, improved governance, and social development.*

*The program creates spaces for collaboration, strengthening coalitions and networks, civil society, private sector, the government, academia, and others to bring about transformative change.*

*Working with these leaders and groups, and armed with technical and political analysis, CfC helps usher in reforms that lead to sustainable and inclusive development, improving the lives of Filipinos.*

# AGRICULTURE, POVERTY, AND PROPERTY RIGHTS IN THE PHILIPPINES



The principal Philippine development challenge is poverty. While some progress has been made, it remained high at 20 percent in 2018.<sup>1</sup> In addition, poverty incidence is much higher in rural areas (36 percent) compared to the urban areas (13 percent).<sup>2</sup> Among the basic sectors, farmers have the highest poverty rate. In 2015, the poverty incidence of farmers was at 34.3 percent, exceeding the national average of 21.6 percent.<sup>3</sup> As such, any effort to address and reduce poverty in the Philippines must focus on rural areas and agriculture.

The rural economy has been characterized for many years by the low income levels of agricultural workers, low levels of rural employment, lack of food security, weak agricultural competitiveness, and an overall high level of rural poverty. The sector employs more than a quarter (26 percent) of the workforce in the country.

Economists have long recognized the importance of increasing productivity and competitiveness

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through investments in agricultural technology and more scientific management systems. However, this straightforward policy prescription often confronts the reality of a complicated Philippine property rights regime. The most glaring example of a policy that hinders investments are two provisions in the 1936 Public Land Act on agricultural titles.

These titles, called agricultural free patents, are land grants awarded to natural-born Filipino

citizens, in actual occupation and cultivation of agricultural lands for 30 years, and who have paid corresponding real property tax on the land.

Between 1986 and 2017, the government issued an estimated 2.6 million agricultural free patents covering approximately 2.8 million hectares.<sup>4</sup> Based on standard economic theory, these parcels should attract considerable investment and be among the most productive agricultural lands as they have titles guaranteed by the Philippine government. In reality, however, these lands are shunned by rural financial institutions. Lacking financing, these lands are often just marginal producers.

To unlock this puzzle of having secure property rights but attracting low investments, FEF undertook a detailed study in 2016<sup>5</sup> that identified two major restrictions that hindered lending and investment in the agricultural lands:



*“These parcels should attract considerable investment and be among the most productive agricultural lands as they have titles guaranteed by the Philippine government. In reality, however, these lands are shunned by rural financial institutions.”*



<sup>1</sup> This is referred to as the proportion of the population living below the poverty line to the total population. See Philippine Statistics Authority Release No. 2019-053. Retrieved from: <https://psa.gov.ph/poverty-press-releases/nid/138411>.

<sup>2</sup> *Farmers, Fishermen and Children Consistently Posted the Highest Poverty Incidence among Basic Sectors*. 30 June 2017. Philippine Statistics Authority Release No. 2017-150. Retrieved from <https://psa.gov.ph/content/farmers-fishermen-and-children-consistently-posted-highest-poverty-incidence-among-basic>

<sup>3</sup> Employment in agriculture data. International Labour Organization, ILOSTAT database. September 2019. Retrieved from <https://data.worldbank.org/indicator/SL.AGR.EMPL.ZS?locations=PH>

<sup>4</sup> Department of Environment and Natural Resources' estimate data (1986 to 2017).

<sup>5</sup> *Freeing the Land Market: How Legal Restrictions Hamper Agricultural Development and Poverty Reduction*. 2016. Foundation for Economic Freedom.

## MAJOR RESTRICTIONS

**1. FIVE-YEAR RESTRICTION ON MORTGAGE AND SALE.** This restriction denies the land patent holders access to the formal credit market as the land cannot be sold, mortgaged, or transferred for five years from when the title is awarded. If the holder wants to use the land in a transaction to finance improvements or capital, it must be done in the informal financial market. Often in these informal transactions, the parcels are undervalued, and the interest rates are higher. The said transaction has the overall effect of reducing the amount of money that could be invested to make the land more productive and increase the income of the holder. The specific provision is in Section 118 of the Commonwealth Act 141 or Public Land Act of 1936.

**2. FIVE-YEAR RIGHT TO REPURCHASE.** The second restriction is the most damaging provision. Section 119 of the Public Land Act states:

*“Every conveyance of land acquired under the free patent or homestead provisions, when proper, shall be subject to repurchase by the applicant, his widow, or legal heirs, within a period of five years from the date of conveyance.”*

In other words, the original title holder of a parcel has the right to buy back the land within five years of the sale. This creates an enormous disincentive to buyers. Even if they bought the land, they would be reluctant to invest it in with the knowledge that over the next five years, the original owners could repurchase the parcel. Banks were even more reluctant to lend to those types of parcels for two reasons. First, the bank is aware of the possibility that the original owners may repurchase the parcel and create a complicated and expensive legal

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case. Second, the condition runs in conflict with foreclosure rules of the banking regulator, the Bangko Sentral ng Pilipinas (BSP) or central bank. In order to foreclose and eventually sell the property, banks must wait for five years, instead of the usual one-year period. But, holding the property penalizes the bank, due to the capital charges that BSP applies.

As one rural banker noted, “we do not lend to agricultural free patents. It seems counterintuitive, but we ask the borrower if they have an untitled parcel rather than an agricultural free patent that can be used as collateral.”

For more than eight decades, these restrictions were implemented, hampering the growth and development of agriculture free patent holders and hindering potential land and agriculture investments in the countryside.

## BROKERING ENGAGEMENTS

Based on the analysis and consultations with farmers, rural banks, government agencies, business organizations, development organizations, academe, and land reform advocates a new legislative priority emerged: amending the Public Land Act of 1936 to remove the five-year restriction on mortgage and sale and the five-year right to repurchase.

Armed with a clear reform agenda, the FEF team began efforts to increasing awareness among legislators of the importance of the reform. They presented the proposed reform and draft bill to several legislators. In the end, Senators Richard Gordon and Bam Aquino filed bills that were referred to the Senate Committee on Environment and Natural Resources. In the House of Representatives, the bills filed by Representatives Joey Salceda, Maximo Rodriguez, Jr., Kit Belmonte, Miro Quimbo, and Arthur Yap were referred to the House Committee on Justice.

With the bills filed, FEF discussed the merits of amending the law with Representative Reynaldo Umali, Chairperson of the House Committee on Justice and Senator Cynthia Villar, Chairperson of the Senate Committee on Environment and Natural Resources. Representative Umali expressed some interest in moving the bill forward. He referred the team to Representative Noli Fuentebella, the head of the sub-committee handling land issues, and directed the Committee Secretary to consult FEF. On the other hand, while the team made numerous attempts to set up a meeting with Senator Villar, the bill did not progress. Given

their experience in dealing with legislative bodies, FEF knew that having committee chairpersons in both chambers championing the bill is crucial. Without these champions, a filed bill can quickly get overshadowed by competing or controversial priorities.

With this knowledge, FEF exerted all efforts to convince Senator Gordon to have the bill retitled and transferred to the Senate Committee on Justice and Human Rights, which the senator also chairs. The FEF team’s quick response to adjust its strategy paid off. In December 2016, Senator Gordon refiled his Agricultural Free Patent Reform bill, Senate Bill (SB) No. 1260<sup>6</sup>, and was referred to the Committee on Justice and Human Rights.

The support of Senator Gordon was a game-changer. In May 2017, propelled by statements of support, such as that from the Rural Bankers Association of the Philippines (RBAP) and leading agricultural economists, the Committee on Justice and Human Rights and the Committee on Environment and Natural Resources called for a public hearing to deliberate the Agricultural Free Patent bills.<sup>7</sup> Among the invited resources speakers were coalition members from different government agencies and organizations: officials from the Land Management Bureau (LMB), the Department of Justice (DOJ), the Land Registration Authority (LRA), RBAP, Arellano University, and Registry of Deeds (ROD). In the same month, the senior senator facilitated the passage of the Agricultural Free Patent Reform bill at the Senate.

<sup>6</sup> Senate Bill No. 1260 “An Act Removing the Restrictions in the Registration of Land Titles Under Sections 118 and 119 of Commonwealth Act No. 141 or Public Land Act, As Amended, On Free Patents Issued Under Section 44 Thereof”. The previously filed bill of Sen. Gordon is Senate Bill No. 101, which proposes to remove the restrictions for Sections 118, 119, 121, 122 and 123.

<sup>7</sup> Under this legislative calendar, there were three Agricultural Free Patent bills filed at the Senate and five bills filed at the House of Representatives.

# ROADBLOCK AT THE HOUSE OF REPRESENTATIVES

While FEF successfully convinced more district and party-list representatives<sup>8</sup> to file the Agricultural Free Patent bill, there was no success in scheduling the hearing for the bill. Requests made to Representative Umali as the Chairperson of the House Committee on Justice, to prioritize hearing the bill did not work. Around this time, the House Committee on Justice's schedule was full to investigate impeachment complaints against former Chief Justice Maria Lourdes Sereno and the imposition of martial law in Mindanao.

The team tried different routes to secure the bill's hearing with the Committee on Justice, such as working with fellow coalition members like RBAP and the Office of Senator Gordon. Finally, in February 2018, the House Committee on Justice scheduled a hearing for the Agricultural Free Patent Reform bill. Coalition members DOJ, LRA, LMB, and RBAP were again invited as resource speakers. Two months after the hearing, the committee approved the committee report and the substitute bill.

Just when the FEF team thought the prospects of progress were positive, a major change in House leadership occurred. Gloria Macapagal Arroyo was elected as the Speaker, replacing

Representative Pantaleon Alvarez. As a result, the leaderships of the various House committees were also changed. These changes could potentially undo all the hard work of building relationships with key legislators. The status of the reform in the legislature was again in jeopardy.

In the end, the unanticipated revamp at the House was a blessing in disguise for the Agricultural Free Patent bill. Representative Paulino Salvador Leachon from the first district of Oriental Mindoro became the new Justice Committee Chair. Representative Leachon is a close political ally of an FEF fellow and a believer in the reform, who was able to help FEF connect with the new chair. House Speaker Gloria Macapagal Arroyo also nudged Representative Leachon to schedule the bill for interpellation on second reading. FEF again worked with the coalition and critical individual allies to secure the bill's approval. By November 2018, Representative Leachon had sponsored and shepherded the bill to its second and third readings. Both Senate and House of Representatives ratified the bill and was submitted for the President's approval. Finally, on 22 February 2019, President Duterte signed the Agricultural Free Patent Reform Act!<sup>9</sup>

<sup>8</sup> Representative Luis Raymund Villafuerte, Jr. filed House Bill No. 6293; Representatives Orestes Salon and Delphine Lee of AGRI Party-list filed House Bill No. 6238; and Representative Ferdinand Hernandez filed House Bill No. 6091.

<sup>9</sup> Republic Act 11231 "An Act Removing the Restrictions Imposed on the Registration, Acquisition, Encumbrance, Alienation, Transfer and Conveyance of Land Covered by Free Patents Under Sections 118, 119 and 121 of Commonwealth Act No. 141, Otherwise Known as the "Public Land Act", As Amended. Retrieved from <https://www.officialgazette.gov.ph/downloads/2019/02feb/20190222-RA-11231-RRD.pdf>

# ANTICIPATED IMPACT

The Agricultural Free Patent Reform Act (RA 11231) stipulates that public agricultural lands awarded to qualified public land applicants shall not be subject to restrictions, encumbrances, conveyances, transfers, or dispositions.

This 2019 law also has a retroactive effect. Any restriction regarding acquisitions, encumbrances, conveyances, transfers, or dispositions imposed on agriculture free patents under Section 44 of Commonwealth Act No. 141, as amended, before the effectivity of the Agricultural Free Patent Reform Act, are lifted.

The new law facilitates transactions related to the 2.5 million agricultural titles, which FEF estimates to value at about Php 387 billion (AUD 11 billion). Agricultural free patent holders can now sell or use their land as collateral at a fair market price at any time. CfC shall work with the concerned government agencies to observe if the new law's anticipated impact will be realized.

Ultimately, the Agricultural Free Patent Reform Act empowers farmers and investors as they can now choose the best economic and social use for their land.

Agricultural Free Patent Reform Act removes the restrictions on agricultural free patents under the Public Land Act of 1936 as follows:

- 1 Five-year prohibition on selling and mortgaging from the issuance of patent (Section 18)
- 2 Five-year right to repurchase the patents within five years from the transfer and conveyances (Section 19)
- 3 Prohibition on corporation, association, or partnership to acquire or own an agricultural free patent (Sec. 121)



<sup>10</sup> *Freeing the Land Market: How Legal Restrictions Hamper Agricultural Development and Poverty Reduction*. 2016. Foundation for Economic Freedom.

# LESSONS LEARNED

Introducing such a potentially transformative reform such as the Agricultural Free Patent Reform Act is a major challenge to development organizations and practitioners. While there are unique and specific circumstances that facilitated the introduction of the law, there are some general lessons that can be drawn from this experience:

**PROBLEM-DRIVEN AND EVIDENCE-BASED POLICYMAKING.** CfC reform partner, FEF, spent a year to study the legal restrictions hampering agricultural development in the country before asking legislators to amend the Public Land Act of 1936. The research confirmed what they have suspected: farmer entrepreneurs owning agricultural free patents are restrained from selling and mortgaging their land.

Furthermore, RBAP revealed that their bank members did not accept agriculture free patents as collateral due to its five-year repurchase provision. It is crucial to take time to listen and understand the realities happening on the ground and to be equipped with facts before drafting a policy. Although the research took considerable time, it established the need to address this issue.

**COALITION'S SUPPORT FROM INCEPTION TO CULMINATION OF THE REFORM.** As FEF examined the legal restrictions, they also reached out to many advocates concerned about land, such as bank associations, academe, and business chambers. An essential addition to the mix was the involvement of government agencies connected to land management: LMB, DOJ, LRA, and ROD. Cultivating the coalitions' ownership of the reform took years as FEF involved these organizations and key individual allies from the inception until the culmination of the policy reform. The coalition members showed their unwavering support by tapping their networks to move the bill forward, and informing the legislators by acting as resource speakers during deliberations at the Senate and House of Representatives.

**FIND YOUR COMMITTED REFORM CHAMPION.** The Agricultural Free Patent Reform bill could have been stalled at the Senate, had Senator Gordon disagreed with retitling and transferring the bill to the Committee on Justice and Human Rights. After its passage at the Senate, Senator Gordon and his office continuously worked on the bill by nudging their House counterpart Committee on Justice to schedule the hearing and pass the bill. Having a senior and decisive Senator as a reform champion was a game-changer – but the engagement with the senator did not happen by chance but through strategic and deliberate efforts from the team.

## CONCLUSIONS

At the start of the paper, we noted the central and critical role of agriculture in reducing poverty in the Philippines. More should be done to complement the Agricultural Free Patent Reform Act. Coalitions for Change continues to explore other opportunities to promote and support reforms that will enhance agricultural productivity further and increase farmers' income to reduce the high poverty rate in the Philippines.



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