FLEXIBLE CASH FARM LEASES, PRACTICAL OPTIONS

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Abstract

Landowners and farmers have found it increasingly hard to agree on an equitable cash rent as crop prices and input costs have experienced significant volatility recently. Cash lease rates aren't public knowledge and don't have any public clearinghouse such as a futures exchange so information on rates is often sketchy. Farmers with full yield and profit information are often reluctant to share this information with the landowner for fear of rent escalation. Landowners knowing there is significant value in "fringe benefits" that farmers provide (snow clearing, rock removal, fence-row maintenance, tiling, etc.) may be reluctant to recognize this value in the negotiation process. Flexible cash leases do allow flexibility but they may not be for everyone. They do require more communication between landowner and farmer. They also require more management and record keeping. These flex leases typically require a sharing of data from the farming operation and have a set of mathematical calculations that need to be performed at the end of the lease period. Since most flex leases require some combination of yield and price, there needs to be verification mechanisms agreed to and written into the lease. The following two examples display two different flex lease methods.

Cash Lease with a Bonus Approach. Tenant and Landowner agree on:

- *Base Rent (and Max Rent?) Base Rent should be below market rent due to landowner upside.*
- *Base Gross Revenue (Agreed upon price x yield combo or Tenant Cost of Production plus X$s?).*
- *How to calculate and verify Actual Year-End Revenue (Yield and Price verification)?*
- *How Extra revenue (Actual Revenue – Base Revenue) is shared? What %?*

Example:

- *Base Rent: $150 (Max: $250),*
- *Base Revenue: $869 (158bpa*$5.50/bu.),*
- *Excess revenue shared: 33% to landowner,*
- *Actual Revenue: $1018 (177bpa*$5.75),*
- *Bonus: ($1018-$869)*33% = $50,*
- *Total Flex Cash Lease Amount: $150 + $50 = $200/acre,*
- *Percent of Gross Income Approach,*

Tenant and Landowner agree on:

1. *Minimum Rent (and Max Rent?) Min. Rent should be below market rent due to landowner upside.*
2. *How to calculate and verify Actual Year-End Revenue (Yield and Price verification).*
3. *Percent of gross income as rent by crop.*

Example:

- *Minimum Rent and Maximum Rent: Minimum$150 and Maximum $250.*
  Percent of Gross Income as Rent: corn – 28%, soybeans – 37%.
  Actual Revenue: corn – $750 (150bpa$5.00), soybeans – $552 (46bpa*$12.00).*
  *Rent: corn -$750*28% = $210/a, soybeans -$552*37% = $205/a*

The verification part of a flex lease is often the trickiest part of the whole arrangement. The price component verification can be easily solved by choosing a market destination for price averaging in the flex lease calculation that is accessible to both tenant and landowner. The difficult parameter to verify in most flex lease calculations is the yield component. Weight tickets, yield maps, bin measurements or crop insurance yield submissions are viable options.

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