

# Intro to Farmland Leases

# Topics

- Land Lease Trends
- Communication
- Understanding & Maintaining the Productivity of Your Farm
- Types of Leases & Figuring a Fair Rent
- Legal Issues in Farm Leases

# Why is it a Good Time to Look at Land Leases?

- Price Volatility
  - Both inputs and commodities
- Land Market
  - Land value (higher)
  - More rented land
- More and more absentee or long distance landowners

## Leasing Indiana Farmland

- Percentage of leased farmland in Indiana is growing
  - 2012 – 53%
  - 2007 – 54%
  - 2002 – 52%
  - 1997 – 51%

Source: Census of Agriculture

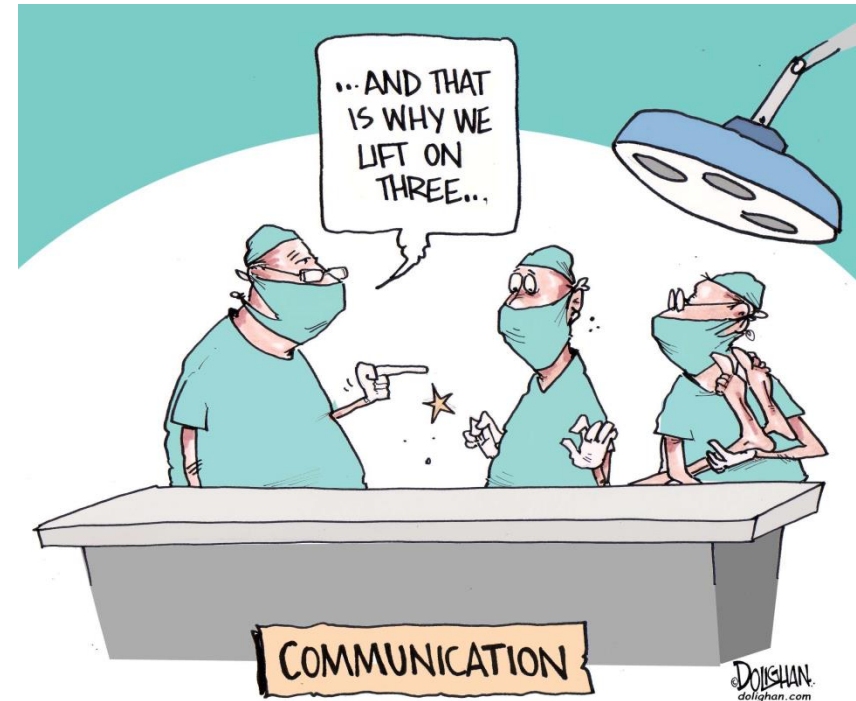
# Volatility

- Weather
- Commodity Prices
- Input Prices

# Communication

# Communication Establishes Trust

- Communication helps to create a good relationship between the landowner and tenant
  - It's important...
    - Both parties clearly understand the terms of the lease.
    - Feel comfortable talking with one another.



Understand each other's values and goals surrounding the land.

# Written vs. Oral Communication

- Oral communication is important
  - Updates throughout the year
  - Maybe hand delivering rent check
  - Depends on agreement, landowner
- But written communication is crucial!
  - **A written contract is a must**, don't rely solely on an oral agreement.



# How Frequently Should You Communicate

- Depends on the landowner
  - Wants, availability
- Should at least be 2-3 times a year
- Communicate early and often
- Don't leave issues unaddressed

# End of the Year Report

- Crops planted
- Yields by crop or by crop and farm tract
- Notable production notes
- Land issues
- A brief description of plans for next year
- In the case of a crop share, a detailed summary of shared expenses
- In the case of a flexible lease, any components of the rent formula

## Working with a New...

### ... Landowner

- Build a relationship
- Ask questions about the history of the land
- Ask about prior lease arrangement
- What are the landlord's expectations?
- Check in more frequently

### ... Tenant

- Build a relationship
- Ask questions about tenant's production practices
- State expectations
- Don't be afraid to ask questions

# Understanding & Maintaining the Productivity of Your Farm

# Understanding & Maintaining the Productivity of Your Farm

- Several factors influence farm productivity
  - Rainfall
  - Drainage
  - Hybrid selection
  - Soil fertility and health
  - Good agronomic practices



# Land is an Asset



- Like any asset-investments need to be made
- Productivity is proportional to investment

# Nutrients Must be Maintained for Good Productivity

- Crops are heavy users of fertilizer, water, and sunlight
- Fertility and pH must be maintained at proper levels
- Crop usage better indicator than soil tests





# Water Management is Key to Productivity

- Water is key to crop yields
- Supplement in dry weather
- Manage excess water through drainage





# Soil Health and Fertility



- Good fertility
- Proper pH
- High organic matter
- Good soil structure
- Reduce compaction

**All leads to greater  
productivity**

# Agronomic Practices

- Best practices lead to greater profit potential
- Water management and soil health best practices are very important
- Timely planting, harvesting, and pest management are key considerations

**The Human Factor: How good is it?**

# What Is a Farm Worth in Rent?

- Opportunity cost
- Markets
- Land
  - Size
  - Quality of land
  - Ease to farm
  - Market forces



# TYPES OF LEASES

# Types of Leases

- Crop-share
- Cash
- Flexible cash

## Types of Leases

# **CROP-SHARE LEASE**

## Crop-share Lease

- Tenant & landowner share some input costs
  - Seed, fertilizer, pesticides
- Tenant pays remaining operating costs
  - Machinery, labor, etc.
- Landowner pays land ownership costs
  - Real estate taxes, maintenance expenses, etc.
- Tenant receives a share of the crop as rent
- Price & yield risk shared

## Crop-share Lease (% Share)

### **50-50 share**

- Input costs shared equally between tenant & landowner
- Crop is shared equally

### **1/3-2/3 share**

- Landowner pays 1/3 of input costs with tenant paying remaining 2/3
- Landowner receives 1/3 of crop with tenant receiving the remaining 2/3

*May be variations in which costs are shared and which are not*



# Crop-share Lease

- Landowner advantages
  - Share in gains from high yields and/or high prices
  - Receive information about crop productivity
  - Direct benefit (via land productivity) from capital improvements such as tile or irrigation
  - Benefit from superior management ability of tenant

# Crop-share Lease

- Tenant advantages
  - Risks due to low yields or prices are shared
  - Less operating capital “tied up”
  - Don’t need to finance cash rent payments

# Crop-share Lease

- Landowner disadvantages
  - Income is variable
  - Must make marketing decisions
  - Often provides a lower return than a cash rent lease
  - More capital tied up than cash rent lease
  - Need to monitor accuracy of expense charges
  - Requires a high degree of trust in tenant
  - Lease needs to be reviewed for fairness as production methods change

# Crop-share Lease

- Tenant Disadvantages
  - Profit from unexpected high yields or prices are shared
  - Requires keeping track of shared expenses
  - Lease needs to be reviewed for fairness as production methods change
  - Need to discuss annual cropping practices to make joint management decisions

# Crop-share Lease

- Challenges
  - What is the correct share?
    - Varies with contribution, technology, cost of inputs, relationship
    - Is the return competitive to cash rent?
  - What items will be shared?

# Types of Leases

## **CASH LEASE**

## Cash Lease

- Tenant pays all operating costs
- Landowner pays all land ownership costs
  - Real estate taxes, maintenance expenses, etc.
- Tenant receives entire crop & government payments
- Landowner receives a fixed rental amount
- Tenant takes all price & yield risk

## Cash Lease

- Landowner advantages
  - Requires less managerial input
  - Reduces concern over accurate division of crops and expense
  - No worry about marketing crops
  - Lessens concerns over variations in prices and yields



# Cash Lease

- Tenant advantages
  - Relative freedom in management decisions
  - Receive full benefit of your management skills and unexpected crop price increases and/or high yields
  - Eliminates division of crops or income from the sale of crops
  - Eliminates the need to keep track of crop expenses

# Cash Lease

- Landowner disadvantages
  - Difficult to negotiate/renegotiate rental rate acceptable to both parties
  - Income could be less than crop share lease in some years
  - Potential for tenant to “mine” the land due to little or no landlord involvement
  - Potential for less production information shared by tenant

# Cash Lease

- Tenant disadvantages
  - Higher risk - Cash rent becomes a fixed cash expense that may be difficult to pay in a poor crop year or with abnormally low prices
  - Cash rents tend to go up as crop yields increase
  - Higher capital costs
    - Pay all the crop production expenses
    - Pay cash rent – half at beginning of year, half at end of year

# Cash Lease

- Challenges
  - What is the correct amount of rent?
    - Varies with grain price, yield, input costs, relationship
  - What is happening to fertility?
  - Is the landowner receiving adequate farm productivity information?

# Cash Lease

- Establishing a Fixed Cash Rental Rate
  - Tenant's residual
  - Landowner's adjusted net-share from crop-share
  - Market approach
  - Return on investment

# Cash Lease – Establishing Rental Rate

- Tenant's residual
  - Estimate how much money is available for rent after variable and fixed costs

Gross revenue(crop sales & government payments)

- operating expenses
  - machinery ownership costs
  - drying & storage
  - operator labor, management, & risk
- = Return to land**

	<b>Corn</b>	<b>Soybeans</b>
<b>Income</b>		
Yield (bu.)	165	50
Price (\$/bu.)	3.50	9.10
Govt. Payment (\$/ac.)	19	19
<b>Total</b>	<b>\$597</b>	<b>\$474</b>
<b>Operating Costs (\$/ac.)</b>		
Fertilizer	144	57
Seed	124	75
Pesticides	43	28
Dryer fuel	26	0
Machinery Fuel & Repairs	47	33
Hauling	17	5
Interest	12	7
Insurance/misc.	33	23
<b>Total</b>	<b>\$446</b>	<b>\$228</b>
Machinery Ownership	71	47
Family & Hired Labor	47	47
<b>Total Costs</b>	<b>\$564</b>	<b>\$322</b>
<b>Return to land</b>	<b>\$33</b>	<b>\$152</b>

# Cash Lease – Establishing Rental Rate

- Landowner's adjusted share
  - Calculates an estimate of the landowner's share under a crop-share lease to determine cash rent amount
    - Use 5-10 year yield average and current harvest time price for revenue estimate
    - Use current estimated crop production expenses



	<b>Corn</b>	<b>Soybeans</b>
<b>Income</b>		
Yield (bu.) (1/2)	83	25
Price (\$/bu.)	3.50	9.10
Govt. Payment (\$/ac.) (1/2)	10	10
<b>Total</b>	<b>\$301</b>	<b>\$238</b>
<b>Operating Costs (\$/ac.)</b>		
Fertilizer (1/2)	72	29
Seed (1/2)	62	38
Pesticides (1/2)	22	14
Dryer fuel (1/2)	13	0
Hauling (1/2)	9	3
Interest (1/2)	6	4
Insurance/misc. (1/2)	17	12
<b>Total expenses paid by owner</b>	<b>\$201</b>	<b>\$100</b>
<b>Net return to owner</b>	<b>\$100</b>	<b>\$138</b>

# Cash Lease – Establishing Rental Rate

- Market approach
  - Rental rate based on current rents in the area
  - Often difficult to obtain a “going rate”
  - “Going rate” does not apply to every situation
  - Potential sources include:
    - Purdue Land Value & Cash Rent Report
    - NASS Cash Rent Values
    - Word of mouth

Table 2. Average estimated Indiana cash rent per acre, (tillable, bare land) 2013 and 2014, Purdue Land Value Survey, June 2014

Area	Land Class	Corn bu/A	Rent/Acre		Change '13-'14 %	Rent/bu. of Corn		Rent as % of June Land Value	
			2013 \$/A	2014 \$/A		2013 \$/bu.	2014 \$/bu.	2013 %	2014 %
North	Top	194	310	297	-4.2%	1.53	1.53	3.3	3.0
	Average	162	228	228	0.0%	1.40	1.41	3.1	2.9
	Poor	130	165	166	0.6%	1.31	1.28	3.0	2.8
Northeast	Top	189	259	261	0.8%	1.41	1.38	2.9	2.8
	Average	160	204	205	0.5%	1.35	1.28	2.9	2.6
	Poor	132	154	159	3.2%	1.26	1.20	2.7	2.6
W. Central	Top	206	350	352	0.6%	1.73	1.71	3.2	3.0
	Average	175	282	291	3.2%	1.65	1.66	3.1	3.0
	Poor	147	222	233	5.0%	1.57	1.59	3.1	3.1
Central	Top	200	294	305	3.7%	1.52	1.53	3.1	2.9
	Average	170	238	248	4.2%	1.47	1.46	2.9	2.9
	Poor	142	188	197	4.8%	1.40	1.39	2.9	2.9
Southwest	Top	189	294	277	-5.8%	1.53	1.47	3.2	3.1
	Average	151	216	204	-5.6%	1.41	1.35	3.0	2.9
	Poor	112	155	143	-7.7%	1.34	1.28	3.2	3.2
Southeast	Top	181	199	186	-6.5%	1.14	1.03	4.1	3.6
	Average	141	152	141	-7.2%	1.06	1.00	3.9	3.2
	Poor	100	110	98	-10.9%	1.02	0.98	3.6	2.9
Indiana	Top	196	294	292	-0.7%	1.52	1.49	3.2	3.0
	Average	163	229	232	1.3%	1.43	1.42	3.1	2.9
	Poor	132	174	179	2.9%	1.37	1.36	3.0	2.9

**COUNTY CASH RENTS, INDIANA, 2010 1/**

County	Cropland Rent		Pastureland Rent	County	Cropland Rent		Pastureland Rent
	Non-Irrigated	Irrigated			Non-irrigated	Irrigated	
<u>Dollars per Acre</u>				<u>Dollars per Acre</u>			
Adams	148.00			Lawrence	102.00		29.00
Allen	140.00		49.00	Madison	147.00		85.50
Bartholomew	146.00		52.50	Marion			
Benton	173.00		41.00	Marshall	110.00		
Blackford	149.00		58.00	Martin	118.00		53.00
Boone	157.00			Miami	144.00		78.00
Brown				Monroe	90.50		26.00
Carroll	177.00			Montgomery	172.00		45.00
Cass	158.00		57.00	Morgan	147.00		59.00
Clark	96.50		59.00	Newton	155.00		
Clay	125.00		33.50	Noble	112.00	154.00	63.50
Clinton	163.00		52.50	Ohio			
Crawford	78.00		25.00	Orange	109.00		
Daviess	156.00		30.50	Owen	115.00		50.00
Dearborn	149.00		14.00	Parke	137.00		73.00

# Cash Lease – Establishing Rental Rate

- Return on investment
  - Multiply estimated current market value of land by expected rate of return
  - Recent cash rent surveys indicate cash rents average 3-4% of market value
  - Imprecise but establishes a range

2014 Purdue Land Value and Cash Rent Survey						
<u>Indiana</u>						
Land Values		Cash Rent			Percent	
Top	9765	Top	292			2.99%
Ave	7996	Ave	232			2.90%
Poor	6160	Poor	179			2.91%
					Ave	<b>2.93%</b>
<u>Southwest IN</u>						
Land Values		Cash Rent			Percent	
Top	9041	Top	277			3.06%
Ave	7006	Ave	204			2.91%
Poor	4513	Poor	143			3.17%
					Ave	<b>3.05%</b>

Land Value	7500		
Rate of return	2.90%	3.00%	3.20%
Estimated rental range	<b>218</b>	<b>225</b>	<b>240</b>

# Now What??

Tenant's Residual	93
Landowner's Adjusted Share	119
Market Approach	204
Return on Investment	225

Negotiate, negotiate, negotiate.....

## Types of Leases

# **FLEXIBLE CASH LEASE**



# Flexible Cash Lease

- Tenant pays all operating costs
- Landowner pays all land ownership costs
  - Real estate taxes, maintenance expenses, etc.
- Tenant receives entire crop & government payments
- Rent amount varies based on price, yield, or gross revenue, etc.

# Flexible Cash Lease

- Advantages & Disadvantages
  - More complicated than fixed cash lease
  - Net income varies for both tenant & landowner
  - Performance depends on terms of lease
    - Base rent
    - Operators guarantee
    - Amount of adjustments above minimum rent
  - Requires careful monitoring

# Flexible Cash Lease

- Types of Flexible Leases
  - Percentage of Gross Revenue
  - Base Rent plus Bonus
  - Base Adjusted for Price
  - Base Adjusted for Yield
  - Base Adjusted for Price & Yield

# Flexible Cash Lease

- Percentage of Gross Revenue
  - Rent amount set at a percentage of gross revenue, usually 25-40%
  - Gross revenue calculated by multiplying actual harvested yield by cash market price
  - Similar to crop share lease without division of costs or harvested crop

# Flexible Cash Lease

- Base Rent plus Bonus
  - A minimum base rent is set, to which a share of revenue above a certain base gross revenue value may be added
  - Minimum base rent should be set lower than a typical fixed cash rent amount
  - Base gross revenue could equal revenue under typical conditions or tenant's cost of production (including base rent)

# Flexible Cash Lease

- Base Adjusted for Price and/or Yield
  - A base rent is set and adjusted based on the price and/or yield of the crop
  - Leases adjusted for only price or only yield may increase tenant's risk
  - If base rent is a minimum rent, it should be set lower than a typical fixed cash lease rate

# Flexible Cash Lease

- Challenges
  - How is a base rent amount determined?
  - What share of gross revenue is used?
  - What is the source of price and yield information?
    - County or farm data
    - When is the data collected?

# Legal Issues in Farm Leases

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# Duration of a lease

## **ORAL OR WRITTEN LEASE**

# Oral Leases

- Oral leases are binding in Indiana
- Advantage: No paperwork
- Disadvantage: Bad memories
- Today's Farming practices are too complicated to leave to memory

**Put it in Writing!**

Does requesting a written lease  
signal a lack of trust?

**Absolutely not!**

# Benefits of a written lease

- It documents the terms of your agreement and provides a basis for avoiding or settling misunderstandings.
- It is an effective antidote for forgetfulness and the passage of time which can alter contracting parties understanding of agreements first entered into perhaps years ago.
- It forces the contracting parties to consider legal and practical issues that otherwise can easily be overlooked. In that way it is a useful planning tool.

# Duration of Lease

- **Annual or Multi-year Lease**
  - More than 3 years – MUST be in writing
  - Any lease should be recorded at Recorder's Office
    - Protects tenant's rights against transfer of land
    - Puts tenant's rights ahead of creditors
  - Annual leases that automatically renew don't have to be recorded every year (first time is enough)

# Recording a Lease

- Recorded (Memorandum of) Lease must contain:
  - Name and address of Landlord
  - Name and address of Tenant
  - Term of Lease
  - Legal description
- You do not have to record the full lease

# What Should Be Covered in a Lease?

## **ELEMENTS OF A LEASE AGREEMENT**

# Elements of a Farm Lease

- The full and legal names and addresses of the parties and their marital status
- A full and correct legal description of the property
  - Identify Tillable and Non-Tillable Acres
- When the lease starts
- When the lease ends
- The date of making the lease
- Amount and terms of payment
- The landlord and tenant share of costs and crops
- Resource contributions of landlord and tenant



## Elements of a Farm Lease (con't)

- Provisions for re-imbusement of unrecovered investments in improvements, growing crops, and inputs made by tenant.
- An exit plan at end of lease
- Termination of lease other than at expiration of lease
- Allowed uses of the leased land
- Whether use of improvements (barns, bins) is included)
- Allowed and required farming and conservation practices

## Elements of a Farm Lease (con't)

- Maintaining fertility & controlling weeds
- Removing crop residues
- Participating in government programs
- Participation in crop insurance
- Maintaining & using facilities, improvements, & drainage
- Tenant's obligation to furnish production records

# Elements of a Lease: Plan for Changes

- Long-running landlord-tenant relationships must be able to adapt to a changing farm economy
- Include provisions for amending the lease
  - Any amendments should be in writing and signed by both parties.
- Include provisions for resolving disputes
- Include a timeline or plan for renegotiating rents

# Elements of a Lease: Other legal matters

- A statement that the lease arrangement is not a partnership
- Signatures of remainder persons if landlord is a life tenant
- Provision requiring tenant to provide adequate liability insurance coverage that specifically protects landowner
- Indemnification Language
- Provision protecting landlord in the event that farming causes environmental damages
- Provision limiting tenant's right to sublease the land without landowner permission

# Elements of a Lease: Other legal matters

- Lease must be signed by both parties
- Lease must be dated
- If recorded - lease must be notarized
- If more than one year – lease must be notarized
- If landlord is out of area – lease should be notarized
- What about Evergreen Leases?

# Talk to an Attorney

- It is a good investment to protect yourself, the other parties to the lease agreement, and your family.
- It is good business practice and an even better risk management strategy.
- ***More money at stake makes more disputes inevitable.***
- Legal issues related to farmland leasing don't end with the lease agreement itself.

# Tenants

## **RIGHTS AND RESPONSIBILITIES**

# Tenant R&R

(Rights and Responsibilities)

- **Rights of Tenants**

- Right determine how land is used
  - When to plant, what to plant, when to harvest
- Rights to government payments
- Right to growing crops (mostly)
  - Doctrine of Emblements
- Right to continue year-to-year, if not otherwise terminated



# Tenant R&R

(Rights and Responsibilities)

- **Tenant Responsibilities**
  - Not to “commit waste”
    - Removal of noxious weeds
    - Preservation of ditches, watercourses, watersheds
  - To maintain fertility
  - To pay rent (or provide crop share)

# Landlord R&R

(Rights and Responsibilities)

- **Landlord Rights**
  - Payment of Rent
    - UCC Lien on crops
  - Right to preservation of land
  - Right to preservation of fertility

# Landlord R&R

(Rights and Responsibilities)

- **Landlord Responsibilities**
  - Cannot sell land in violation of Tenant rights
  - Allow Tenant “quiet enjoyment” of land
  - Payment of property taxes

# Other Rights and Responsibilities

- Who pays for lime (long-term fertility)
  - Sliding reimbursement for early termination of lease
- Who makes repairs (buildings, fences, ditches)
  - Major repairs
  - Minor repairs
  - Mowing roadsides, general weed control
- Fence rows and trees
- Hunting, Fishing, Boating

# Other Rights and Responsibilities

- Access to the Field
  - Off the road, use of easement
  - Storing equipment
- Third parties – who controls/enforces?
  - Recreational users
  - Mineral rights and leases
  - Wind Turbines – Cell Towers
  - Easements and Cemeteries
    - Access Easements
    - Conservation Easements

# Issues and Concerns

## **WHEN LEASES GO WRONG**

# When Leases Go Wrong

- Oral lease for a term > 3 years
- Any lease that is not recorded
- When LL sells the land
  - What are the Tenant's Rights?
- When LL is bankrupt
  - What are the Tenant's Rights?

# When Leases Go Wrong

- Failure to include termination or notice due dates
  - Confusion as to whether the lease will continue for another year
  - Legal notice by December 1
- It's the Tenant's responsibility to make sure his rights are protected (*aka – Get it in Writing!*)



# What Happens at the End of a Lease?

## **TERMINATION OF LEASES**

# When Leases End - Termination

- **Termination provisions**
  - Notice must be given > 3 months before end of lease
    - UNLESS – Lease is for a specific term, the tenant commits waste, tenant refuses to pay, tenant is at sufferance
- **Failure to give notice timely =**
  - NO Termination

# Good Landlord-Tenant Relationships

## **PRESERVING THE RELATIONSHIP**

# Lease Tips

- **Don't let a farm lease get "stale"**
  - Maintain regular contact with LL/T
  - Foster a good and friendly relationship
  - Discuss rent arrangement at least annually
  
- **Provide documentation**
  - 1099 for rent payments (individuals only)
  - Fertility/Soil Test records
  - Productivity Records

# Lease Tips

- **Provide Education to Landlord**
  - Landlords may be far removed from the farm and not understand customary practices
  - Landlords may not understand that different farms have different values for rent and different challenges for farming
- Good relationships +
- **Good communications** =
- ***Long-Term and Profitable Leases***

# Summary – Legal Leases

- Written
- Type
- Terms
- Termination
- Payment
- LL Rights
- T Rights

## Conclusion

- *Common sense*
- *Staying informed*
- *Following good business practices*
- *Communicating*
- *Investing in competent advice*

***Will greatly increase the sense of security and satisfaction of all parties to farmland leases.***

# More Resources

- More information and sample lease forms available at **North Central Farm Management Extension Committee** website:

<http://AgLease101.org>

- **Purdue Extension Land Lease Website**

[www.agecon.purdue.edu](http://www.agecon.purdue.edu)

- **Iowa State Ag Decision Maker Website**

[www.extension.iastate.edu/agdm](http://www.extension.iastate.edu/agdm)





**Questions? Answers?**

***Thank you for your attention***

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