

Flexible Farm Leases

Cash Rent Surveys

AAEA Extension Section



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Problem:



- ❖ Cash rent leases must be negotiated a year or more before actual yields and prices are known.
- ❖ Prices and yields are very unpredictable

Solution: a **flexible lease contract**

Advantages

- ⌘ Risks and profits are shared
- ⌘ Rent adjusts automatically to economic returns to the land and tenant's ability to pay
- ⌘ No need to renegotiate each year
- ⌘ Owner not involved in paying input costs
- ⌘ Owner not involved in grain marketing

Possible Drawbacks

- Landowner may desire a fixed income.
- More complex.
- More trust required.
- Tenant's actual selling price may be different than the one used to set the rent.
- Tenant gives up some yield advantage due to superior management.

Types of Flexible Leases

- Rent varies with yield, only
- Rent varies with price, only
- Rent varies with both price and yield
 - Rent = percent of gross income
 - Rent = base rent plus a bonus
 - Rent = base rent x price index x yield index

Value of Fixed Number of Bushels

- Cash rent is equal to 10 bushels of wheat
- Actual price is \$4.50
- Rent = \$45
- Price risk is shared
- Works best in areas where yield has very little volatility.

Fixed Price per Bushel of Yield

- Cash rent is equal to \$1.50 per bushel of corn
- Actual yield is 172 bushels per acre
- Rent = \$258 per acre
- Yield risk is shared.
- Works best in areas where price has very little volatility.
- Works best when price doesn't matter, e.g. crop is all fed to livestock.

Problems?



- ❖ If price and yield are negatively correlated, rent may increase but gross revenue may not.
- ❖ Flexing rent based on gross income ties it to the tenant's ability to pay.

Share of Gross Income

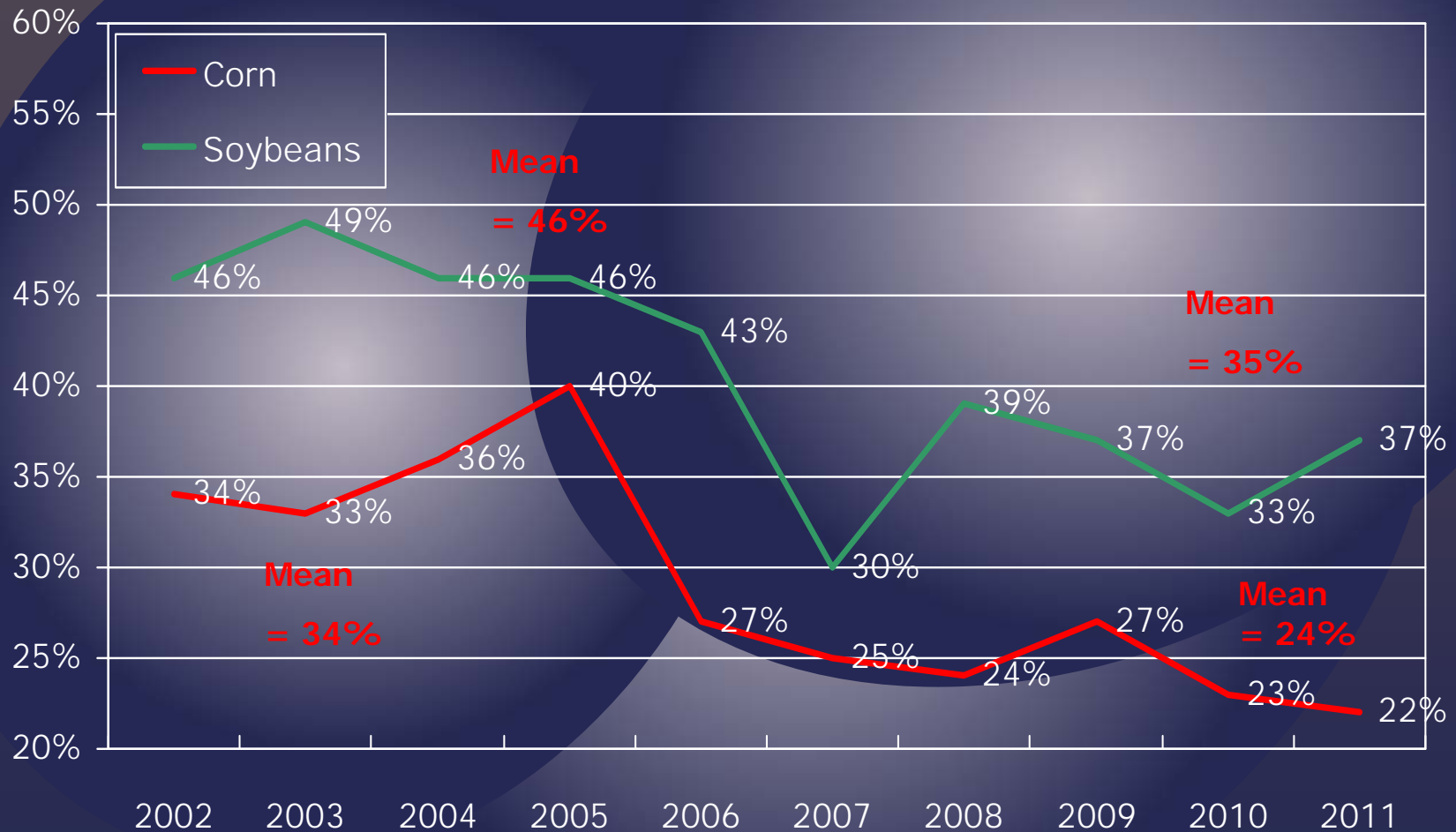
Example--Corn



- Cash rent is equal to 30% of gross income
- Actual yield is 160 bu. of corn
- Harvest market price is \$5.00
- Gross income is $(160 \text{ bu.} \times \$5.00) = \$800$ per acre
- Rent is $30\% \times \$800$, or **\$240** per acre
- If price rises to \$6.50, and yield is the same, rent increases to **\$312**.

Cash Rent as % of Gross Income

Iowa Average Yield x Oct.-Dec. Cash Price



Base Rent plus Bonus

Example--Soybeans

- Rent is \$200 plus half the gross income in excess of \$500 per acre
- Actual price is \$12.50, actual yield is 52 bu.
- Gross income is \$650
- Bonus is $\$150 \times 1/2 = \75
- Total rent is $\$200 + \$75 = \$275$ per acre

Base Rent plus Bonus

- Base rent could be “old” rent levels (before 2011)
- Base revenue could be “old” price levels
- Base revenue could be costs of production, including base rent
- May use tenant’s actual costs, or state Extension budgets
- Shares cost risk, as well (like crop share)

Base Rent Times Index--Example

- Base rent = \$200
- Base price = \$10/bu. (soybeans)
- Base yield = 45 bu/acre
- Actual price = \$12/bu.
- Actual yield = 40 bu/acre

- Rent = $\$200 \times (12 / 10) \times (40 / 44) = \$218/\text{acre}$

Determining the Actual Yield

- Scale tickets when crop is delivered
- Combine yield monitors or weigh wagons in field
- Storage bin capacities
- Correct to standard moisture
- What if crop is sold after harvest?
- Use crop insurance data



What Causes High Yields?

- Land productivity
- Weather
- Tenant's management ability
 - Should an above-average tenant have to pay more rent?
 - Could use county average yield instead (but not available immediately)

Determining the Actual Price



- ⌘ Cash price at local elevator/processor
- ⌘ Take the average for several dates near harvest or when rent is paid
- ⌘ Could use pre-harvest prices, too
- ⌘ Don't use post-harvest prices unless owner provides storage
- ⌘ Could use FSA posted county price
- ⌘ Could use crop insurance harvest price
- ⌘ Must agree on dates, location

Include Crop insurance Payments in Gross Income?

- Does land owner have downside risk?
- If there is a minimum rent, it may not matter
- If ins. payments are included, use net payments
- E.g. deduct premiums, even in years of no indemnity payments
- Allows landowner to “insure” a minimum rent

Include Government Payments in Gross Income?

- ⌘ If rent depends on farm yield, FSA may require sharing **direct payments**.
- ⌘ Revenue support payments (SURE, ACRE)?
- ⌘ New farm bill?

Flexible Farm Leases



- Record the rent formula in writing.
- Test with several examples.
- Develop a table of possible results
- For examples of flexible cash leases see
Ag Decision Maker file C2-22
www.extension.iastate.edu/agdm/

Cash Rent Surveys

- ❖ National Ag Statistics Service (NASS)
- ❖ University surveys
- ❖ Farm Business Association data

NASS Surveys



- & Survey farm operators
- & Summarize by county
- & Ask total \$ paid and acres, or rent per acre
- & Dryland crop, irrigated crop, pasture
- & Excludes land rented from relatives
- & Published in August

University Surveys (Iowa State)

- Survey landowners, tenants, professional farm managers, lenders (1,419 responses)
 - Farm managers society membership list
 - Iowa Bankers Association ag mailing list
 - Extension county staff and councils
 - Registration lists from Extension leasing meetings
 - EWG farm payment data base
 - FSA farm program participant list

“Typical” rates in your county for:

- High, medium, low third quality corn/soybeans
- Small grains, hay, pasture
- Pasture by AUM
- Grazing corn stalks
- Hunting rights

Do not collect individual farm rents.

Respondent Bias?

Average cash rent reported (corn & beans)

- | | |
|-------------------------------|-------|
| ▪ Operators (37%) | \$251 |
| ▪ Lenders, others (19%) | \$263 |
| ▪ Landowners (28%) | \$259 |
| ▪ Professional managers (16%) | \$290 |

ISU versus NASS Results (2011)

- ISU data weighted for all crops
- ISU rent was higher than NASS in all 99 counties
- Average difference was 13 %. Ranged from 1% to 37% by county.
- Reasons?
 - NASS samples farmers only (bias?)
 - ISU is an “opinion” survey
 - “Marginal” rents versus “average” rents

Questions?

