Fixed and Flexible Cash Rental Arrangements for Your Farm – AgLease 101 publication brief summary

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This provides a summary of what is covered in the full-text publication, "Fixed and Flexible Cash Rental Arrangements for Your Farm" located in the AgLease 101 document library **aglease101.org** – a publication to help operators and landowners develop equitable cash-rent arrangements and assist them in making sound decisions based on an equitable evaluation of resources.

Part I Fixed cash-rent lease arrangement – Advantages and disadvantages

A cash rent lease is a fixed agreement in which a landowner receives a pre-determined payment from the farmer to rent the farmland —it does not change based on crop, yield, or market prices.

There are both advantages and disadvantages to cash rent arrangements for the landowner and the land operator. For the landowner, less (perhaps no) managerial input is required than with other leasing arrangements and bears no price, cost, or production risks. Yet determining a cash-rent amount acceptable to both parties can be difficult and in average or above-average years, the landowner may receive less net income than from crop-share rent. For the operator, compared to land ownership, less capital is tied up in the land asset. Yet the operator must supply all the operating capital needed to purchase crop inputs, as well as to pay any of the cash rent that is due in advance and cash rental rates tend to trend upward as crop yields increase, even though most of the yield increases may be a result of managerial skills. More details and points to consider in deciding whether the fixed cash rental arrangement fits your situation are outlined in Part 1 of this **AgLease101.org** document.

Part II How to develop an equitable fixed cash rental rate.

A number of factors affect cash rental rates. Ultimately, supply and demand of cropland for rent will determine the cash rental rate for each parcel. The expected return from producing crops on a farm parcel is the overriding factor in determining the demand for a farm. Land quality, variability and fertility, previous crop, size and shape of fields, and location are all important factors. Conditions placed on the lease by the landowner or special contracts that are tied to the farm that restrict the operator may negatively impact cash rents, while other examples may positively affect cash rents such as high value crop contracts.

Approaches to cash rental agreements: **Aglease101.org** provides an overview of the following approaches to cash-rental agreements, including worksheet examples:

- Cash-Rent Market Approach – This method requires knowledge of cash rents being paid for farms in the area and may use survey data such that conducted by the National Agricultural Statistics Service (NASS).
- Landowner's Ownership Cost – Under this approach, the landowner calculates the cost of ownership for the property as a basis for rent, including taxes and land development.
- Landowner's Adjusted Net-Share Rent – This method assumes the rent value should be comparable to the net return a landowner receives under a crop-share lease.
- Operator's Net Return to Land – With this method operators budget how much money will be available to pay for rent after expenses have been deducted from the gross value of crops.
- Percent of Land Value – Owners look for a rate of return commensurate with other types of investments, adjusted for differences in risk, of a similar holding period.
- Percent of Gross Revenue – Establishes a cash rental rate equal to a fixed percent of the expected gross revenue produced from the rented land.
- Dollars per Bushel of Production – Based on a constant yield, this method can be useful for adjusting the rental rate for differences in productivity among farms in a county or region.

Part III How to develop a flexible cash rent lease and their advantages and disadvantages

Flexible-cash lease agreements involve the operator paying the landowner a predetermined cash fee adjusted for changes in prices and/or yields. The landowner has increased opportunities to share in additional income under a flexible-cash lease agreement when compared to a fixed-cash agreement, and in-turn takes on more responsibility for the risks. For the operator, less risk is assumed and cash-rent expense is lower if crop prices or yields are less than normal. Calculating flexible cash rent requires more communication and management from both parties regarding how to verify the factors that are used to set the rent.
The **AgLease101.org** document provides details and examples for the different methods of flexing cash rent. Cash rents are flexed primarily by: 1) changes in crop price only 2) changes in crop yields only 3) both crop price changes and yield variations or 4) changes in cost of inputs.

Part IV The importance of putting the agreement in writing

The details of how the rent will be determined should be clearly specified in a written lease agreement. Including one or two examples with different prices and yields is helpful, as well. Advantages of a written agreement are:

- Encourages a detailed discussion of the agreement, leading to better understanding by both parties.
- Serves as a reminder of the items originally agreed upon.
- Provides a valuable guide for the heirs if either the operator or landowner dies.