



# Farm Lease Letter

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Letter No. 5

FLEXIBLE CASH LEASE

July 2000

In periods of volatile farm profit or changeable commodity prices, previously determined fixed dollar cash rental rates prove unsatisfactory. The landlord may be dissatisfied when he does not share the increased income which results when prices or yields increase. In periods of locally poor yields, inflating costs or declining commodity price, the tenant, having assumed all risks, can be caught in a financial squeeze.

A flexible cash lease can combine some of the simplicity of the fixed cash lease with some of the flexibility of the crop share lease.

A flexible cash lease varies the amount of rent per acre as prices of farm products and/or yields change. This letter outlines some of the more commonly used flexible cash lease types and some of the considerations in developing a suitable flexible cash lease.

Flexible cash rent usually pertains only to the rent charges for cropland. Rents for pasture, buildings and hay may be on a fixed cash rent basis even though the rent for cropland is flexible.

## CONSIDERATIONS IN A FLEXIBLE CASH LEASE

- Unless the lease reflects differences in both yield and prices, it may not decrease risk as compared to a fixed cash lease.
- The parties still must arrive at a base rental value in some cases.
- If price differences are to be reflected in a cash rent, the lease needs to state specifically the method, time(s) and location for price determination.
- If yield differences are to be reflected in the cash rent, the lease should state how yields will be determined.
- In periods of changing technology and costs of crop production, it is advisable to reappraise the leasing agreement periodically.
- If the terms of a rental agreement shift more risk to one of the parties, it should also give a higher long-term potential return to the party with the increased risk.

### DEVELOPING A FLEXIBLE CASH LEASE

There is no simple formula or “rule of thumb” for developing a suitable flexible cash lease. The key variables are yields, prices and production costs. Most flexible cash leases do not take changes in production costs during the lease year into account, however. Ideally, each lease needs to be tailored to fit the specific situation.

One method of getting at the provisions of a flexible cash lease is to compare it with a cropshare lease to determine how the returns to the landlord and tenant compare.

Another method is to use several assumptions about the price and/or yield variables within the lease and budget out the potential return to the parties involved to see whether they come within the guidelines established by the landlord and tenant for the lease.

### TYPES OF FLEXIBLE LEASES

Flexible cash leases are most satisfactory if developed specifically for each situation. There are, however, a number of commonly used types which can be used as a basis for the development of the specific lease.

### NET PERCENTAGE LEASE

This type of lease is similar to the 50-50 crop share lease except that the tenant pays all of the production expenses. Landowner and tenant share yield and price risk and the landowner, typically, receives a percentage of the crop. The exact percentage share depends on the type of crop to be grown and the productivity of the resources to be used in production of the crop. An equitable percentage share can be determined by comparing the returns to those received under a 50-50 crop share lease. Generally, the landowner would

receive 33 to 38% of the gross value of corn and 35 to 45% of the gross value of soybeans. Transition Payments are shared on the same basis as the crop. The percentage share received from highly productive land would be higher than from less productive land.

The level of rent under this lease varies with the yield and price of the crop similarly to the crop share lease. However, typically the level of rent does not vary as much with changes in the value of crop production as does the crop share lease.

### PRICE YIELD SHARE

$$\text{Rent} = \text{base rent} \times \frac{\text{actual yield}}{\text{base yield}} \times \frac{\text{actual price}}{\text{base price}}$$

Under this type of lease, the rent paid will vary as the actual prices and yields are compared to a base price and yield.

Base rent should be established at a level that will provide an acceptable rent when price and yield are at a level that is typical for the farm in question.

Base yield can be the average of the previous 5 or more years for the farm. Base price can be an average price for a similar period of years.

Careful consideration needs to be given to determination of the base rent, yield, and price factors when developing a price and yield share lease.



It is important for both tenant and landlord to evaluate the potential impact of the various types of leases under consideration. This should be done at extremes in yield and price as well as at most-likely levels.

The example lease situations in the following tables will provide a comparison of the rents that would typically be expected with various price levels. Three potential yield levels are also illustrated to demonstrate the impact of changes of yield capability with various leases. It must also be remembered that increased prices are often the

result of reduced supplies resulting from lower than normal yields.

The typical crop share situation is provided as a basis for comparison. As all situations result in the same total crop production per acre each \$1 change in rent to the landlord will result in a \$1 change in the opposite direction for the tenant. Grain storage and property taxes have not been deducted in arriving at these rent figures.

**CORN**  
**COMPARISON OF RENTS WITH CROPSHARE AND**  
**VARIOUS FLEXIBLE CASH LEASES \$ PER ACRE**

Assumes 125/acre base corn yield and 50% corn base

Crop Price	50-50 Crop Share 1/	% of crop and transition payment 2/	Price and yield rent 3/
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**Corn Yield = 125 Bu. per acre**

\$2.00	\$ 73.70	\$ 93.45	\$ 99.43
\$2.25	\$ 88.70	\$104.39	\$111.86
\$2.50	\$104.32	\$115.33	\$124.29

**Corn Yield = 95 Bu. per acre**

\$2.00	\$ 43.07	\$ 72.45	\$ 75.57
\$2.25	\$ 54.95	\$ 80.76	\$ 85.02
\$2.50	\$ 66.82	\$ 89.08	\$ 94.46

**Corn Yield = 145 Bu. per acre**

\$2.00	\$ 93.07	\$107.45	\$115.34
\$2.25	\$111.20	\$120.14	\$129.76
\$2.50	\$129.32	\$132.83	\$144.18

**SOYBEANS**  
**COMPARISON OF RENTS WITH CROPSHARE AND**  
**VARIOUS FLEXIBLE CASH LEASES \$ PER ACRE**

Assumes 125/acre base corn yield and 50% corn base

Crop Price	50-50 Crop Share 1/	% of crop and transition Payment 2/	Price and yield rent 3/
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**Soybean Yield = 45 Bu. per acre**

\$5.00	\$ 76.28	\$ 89.54	\$ 96.48
\$5.50	\$ 87.53	\$ 97.87	\$106.12
\$6.00	\$ 98.78	\$106.19	\$115.77

**Soybean Yield = 35 Bu. per acre**

\$5.00	\$ 51.28	\$ 71.04	\$ 75.04
\$5.50	\$ 60.03	\$ 77.52	\$ 82.54
\$6.00	\$ 68.78	\$ 83.99	\$ 90.04

**Soybean Yield = 55 Bu. per acre**

\$5.00	\$101.28	\$108.04	\$117.92
\$5.50	\$115.03	\$118.22	\$129.71
\$6.00	\$128.78	\$128.39	\$141.50

- 1/ Gross income (including transition payments) were shared 50-50. Landlord's share of production costs of \$60.43 for corn and \$44.72 for soybeans were subtracted from gross income.
- 2/ Flexible cash lease under which tenant pays all input costs and landlord receives a percentage of the value of the crop as rent plus an equal percentage of the transition payments. In these examples, 35% of the crop is used for corn; for soybeans 37% is used.
- 3/ Assumes \$115 base rent, five year average corn and soybean yields of 122 bu. corn and 45 bu. soybeans, and 5-yr. average corn and soybean prices of \$2.37 and \$5.96.