Farmland Leasing Arrangements

Craig Chase, Field Specialist
Farm & Ag Business Management
Session Topics

• Land Values
• Cash Rental Rates
• Leasing Practices
• Crop-Share Leases
• Calculating a Cash Rent Lease
• Flexible Cash Leases
Background

• Land values have been increasing for the past several years. Record levels for each of the past 5 years.

• Increases fueled primarily by poor overall economy, low interest rates and attractiveness of land investment. Investors were more important in the market the past several years.
Background

• Bioeconomy has created a boom in the land market since fall 2006.
• Land value increases are continuing at a rapid rate.
• Existing farmers are becoming more active participants.
• Land value has more than doubled since 2000.
Ag Decision Maker (AgDM)
An agricultural economics and business web site.

New Information

June Updates

Newsletters
Ag Decision Maker Newsletter (pdf)
- Global warming - more on bio-fuels -- Eugene Takie and Don Hofstrand
- 2008 crop insurance decisions and dates -- Steven D. Johnson
- Value-added business success factors -- the role of local infrastructure and support -- Don Senechal and Nancy Hodur

Iowa Farm Outlook Newsletter (pdf)
Livestock: Living With Higher Feed Costs
Grain: Assessing Corn and Soybean Market Fundamentals
Dairy: March Milk Up 2.5%, Cheese Hits Record Prices

New and Updated Files
- Crops -- Costs and Returns:
  - Organic Crop Production Enterprise Budgets -- A1-18
- Livestock -- Costs and Returns:
Whole Farm Decisions - Land Values

Many of the Information Files listed below are accompanied by companion tools such as Decision Tools, Teaching Activities, and Voiced Media Presentations.

Surveys

Information Files
- Farmland Value Survey (Iowa State University) -- C2-70
- Historic Farmland Values -- C2-72
- Farmland Value Survey (Realtors Land Institute) -- C2-75

Other Surveys
- Federal Reserve Bank of Chicago
- USDA Agricultural Land Values and Cash Rent

Newsletter Articles
- Average value of Iowa farmland tops $3,900 an acre in 2007 survey -- January 2008
- Iowa farmland value at record level for fourth year in a row -- January 2007
- Comparing the stock market and Iowa land values: A question of timing -- June 2005
- Trends in Iowa farmland ownership -- October 2004

Investment Analysis

Information Files
- The Do's and Don'ts of Sealed Bid Auctions -- C2-81

Newsletter Articles
- Returns to farmland ownership -- October 2006
- What will happen to the value of farmland over the next several years? -- July 2005
Iowa Farmland Value Surveys

- Iowa State University Extension
  - conducted annually around November 1st
  - mailed survey sent to 1,100 licensed real estate brokers
  - usually 500-600 responses
  - released in mid-December

- Federal Reserve Bank of Chicago
  - quarterly survey of ag lenders by state
  - http://www.chicagofed.org/economic_research_and_data/ag_letter.cfm

- Realtors Land Institute
  - semi-annual survey (March and September)
  - compares land classification by corn production
  - includes pasture and timber land
Average Values All Grades
1950-2007
Percentage Changes

- Increased up to 20%
- Increased 20.1 to 22.5%
- Increased 22.6 to 25.0%
- Increased 25.1% or more
Recent Land Value Estimates

• Chicago Fed 17% increase April to April
• RLI 9.5% increase September to March

Percent change in dollar value of “good” farmland

Top: January 1, 2008 to April 1, 2008
Bottom: April 1, 2007 to April 1, 2008

<table>
<thead>
<tr>
<th>State</th>
<th>January 1, 2008 to April 1, 2008</th>
<th>April 1, 2007 to April 1, 2008</th>
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<tr>
<td>Illinois</td>
<td>+4</td>
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<td>Indiana</td>
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<td>+10</td>
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<tr>
<td>Iowa</td>
<td>+1</td>
<td>+17</td>
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<tr>
<td>Michigan</td>
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<td>+17</td>
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<tr>
<td>Wisconsin</td>
<td>+6</td>
<td>+10</td>
</tr>
<tr>
<td>Seventh District</td>
<td>+2</td>
<td>+14</td>
</tr>
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</table>
Whole Farm Decisions - Leasing

Rental Rate Surveys

Information Files
- Iowa Farmland Rental Rates (USDA) -- C2-09
- Farmland Cash Rental Rate Survey (Iowa State University) -- C2-10
- Historic County Cropland Rental Rates -- C2-11
- 2002 Building Rental and Contracting Rates -- C2-17
- Historic Building Rental and Contracting Rates -- C2-18

Newsletter Articles
- Grazing survey indicates which counties have highest, lowest rental rates per acre -- October 2007
- Cash rental rates jump in 2007 -- May 2007
- Cash rental rates continue to climb in 2005 -- June 2005
- Cash rent acres are increasing -- July 2003
- Modest gains for cash rental rates -- May 2003

Leasing Forms

Information Files
- Iowa Farm Lease Form -- C2-12
- Iowa Cash Rent Farm Lease (Short Form) -- C2-16
- Midwest Plan Service Lease Forms
- Iowa Farm Lease Termination Notice (Iowa Bar)
Percent of Farmland Rented by the Top Reasons for Choosing the Tenant

- Beginning farmer
- Family
- Good farmer
- Honesty
- Financially stable
- Know personally
- Good conservation
- Can work with
Percent of Crop Share Acres by Category with Equal Division Between Tenant and Landlord

- Yield: 90%
- Seed: 80%
- Fertilizer: 80%
- Custom fert. application: 60%
- Herbicides: 80%
- Lime: 70%
- Drying: 80%

IOWA STATE UNIVERSITY
University Extension
## Crop Share 50-50 Lease

<table>
<thead>
<tr>
<th>Landlord</th>
<th>Tenant</th>
</tr>
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<tbody>
<tr>
<td>Land</td>
<td>Labor</td>
</tr>
<tr>
<td>½ inputs</td>
<td>½ inputs</td>
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<tr>
<td></td>
<td>Machinery</td>
</tr>
<tr>
<td></td>
<td>Management</td>
</tr>
<tr>
<td>½ income</td>
<td>½ income</td>
</tr>
</tbody>
</table>

*Image Source: Iowa State University, University Extension*
Quick Overview

• From the Owner’s perspective:
  – Which lease is least volatile from year to year?

• From the Tenant’s perspective:
  – Which lease is most volatile from year to year?
Putting a Lease Together

• Determine the goals for each party
  – production with the highest potential return
  – fair return to each party
  – continuity of income year to year
  – minimize risk
  – improve communication skills

• **Put the agreement in writing** -

• Both parties should be accountable to the lease arrangements established
Improving Negotiation Skills

• Focus on win-win situations
• Don’t underestimate your position at the bargaining table
• Formulate a resistance point
Determining A “Fair” Cash Rent Value
Supporting Information

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
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<tbody>
<tr>
<td>Location</td>
<td>Cerro Gordo County</td>
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<tr>
<td>Tillable Acres:</td>
<td>400 Acres</td>
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<tr>
<td>Corn Yield:</td>
<td>175 bu/Acre</td>
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<tr>
<td>Soybean Yield:</td>
<td>45 bu/A</td>
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<tr>
<td>Corn Suitability Rating:</td>
<td>78 CSR</td>
</tr>
</tbody>
</table>
Calculating Cash Rent Values

Cash Rent Market Approach
ISU Extension Publication FM 1851 – *Cash Rental Rates for Iowa 2008 Survey* (released in June)

Three Methods for Determining Cash Rent Values

- Typical Cash Rent
- Average Rent for Production
- Average Rent for Corn Suitability Rating (CSR)
Calculating Cash Rent

1. Typical Cash Rent

Select the Area of the State/County

Area 3 County Cerro Gordo
Determine Overall average $ 200

High Quality Third = $ 238
Middle Quality Third = $ 204
Low Quality Third = $ 159
Calculating Cash Rent

2 a. Average Rents Per Unit – Corn Yield

Select the Area of the State/County – Cerro Gordo

Determine Average Rent for Corn

Farm’s Average Corn Yield (bu/A) 175
Times rent per bushel of Corn yield $ 1.17
Equals the Average Rent for Corn Acre $ 205
Calculating Cash Rent

2 b. Average Rents Per Unit – Soybean Yield

Select the Area of the State/County – Cerro Gordo

Determine Average Rent for Soybeans

Farm’s Average Soybean Yield (bu/A) 45
Times rent per bushel of Soybean yield $4.45
Equals the Average Rent for Soybean Acres $200
Calculating Cash Rent

2. Average Rents Per Unit – Corn & Soybeans

Add the Average Rent for Both – Cerro Gordo

Corn Average Rent $ 205
Soybean Average Rent $ 200

Average Rent Corn & Soybeans $ 203
Using Corn Suitability Rating (CSR)

3. Average Rents Per CSR Index Point

Select the Area of the State/County – Cerro Gordo

Determine the Average Cash Rent using CSR

Farm’s Average Corn Suitability Rating 78
Times rent per CSR index point $2.56
Equals the Average Rent for all Row Crop Acres $ 200

Source: ISU Extension Publication FM-1851
Leasing Opportunity

<table>
<thead>
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<th>Soil Type</th>
<th>Acres</th>
<th>Percent</th>
<th>CSR</th>
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<tr>
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<td>61.47</td>
<td>23.2%</td>
<td>85</td>
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<tr>
<td>248</td>
<td>17.72</td>
<td>6.7%</td>
<td>60</td>
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<tr>
<td>T368</td>
<td>16.70</td>
<td>6.3%</td>
<td>90</td>
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<td>212</td>
<td>11.71</td>
<td>4.4%</td>
<td>91</td>
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<td>T369</td>
<td>87.78</td>
<td>33.1%</td>
<td>85</td>
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<tr>
<td>133</td>
<td>9.69</td>
<td>3.7%</td>
<td>80</td>
</tr>
<tr>
<td>220</td>
<td>60.11</td>
<td>22.7%</td>
<td>85</td>
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<tr>
<td><strong>Totals</strong></td>
<td><strong>265.19</strong></td>
<td><strong>100.0%</strong></td>
<td><strong>83.73</strong></td>
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</tbody>
</table>

Iowa Corn Suitability Rating based yield estimation:
179 bushels per acre
Overall Average

Average all 3 Methods – Cerro Gordo

Method 1: Typical Cash Rent $ 200
Method 2: Average Rents per Unit $ 203
Method 3: Average Rents per CSR Index Point $ 200

Total all Methods and divide by 3 $201 /A

$201 /A X 400 Tillable Acres = $80,400

Source: ISU Extension Publication FM-1851
Cash Lease Calculations

Gross Income Method
Tenant Residual Method
Crop Share Method
Return on Investment Method
Assumptions

• 400 crop acres
• 175 bushel corn yield
• 45 bushel Soybean yield
• Corn Market Price - $5.80  $3.50 July 07
• Soybean Market Price - $13.50  $8.70 July 07
• Direct Government Payments average $22.00 / acre
Share of Gross Income

CORN:  \( (175 \text{ bu} \times $5.80) + $22 = $1,037 \)

SOYBEANS:  \( (45 \text{ bu} \times $13.50) + $22 = $630 \)

Iowa cash rents typically are equal to about 30 to 40 percent of the gross income from producing corn, and 35 to 45 percent of the gross income from producing soybeans.

Cash Rental Rate

4a. CORN:  \( $1,037/\text{ac} \times 35\% = $363 \)

4b. SOYBEANS:  \( $630/\text{ac} \times 40\% = $252 \)

Average  \( $ 308 \)
Tenant Residual Method

CORN: \( \$1,037 - \$498 = \$539 \)

SOYBEAN: \( \$630 - \$319 = \$311 \)

Average: \$425

30% lower prices or lower yield \$174
20% lower prices or lower yield \$258
Crop Share Method 50-50 Share

Corn:
50% of gross minus owner’s costs
$519 - $164 = $355

Soybeans:
50% of gross minus owner’s costs
$315 - $96 = $219

Average: $287

(1) The owner is assumed to pay 50 percent of the costs for seed, fertilizer, lime, pesticides, crop insurance, interest and miscellaneous, and drying and storage.
Return on Investment Method

Iowa farm estimated to have a market value of $5,000 per acre. Expected Rent: \((4.8\%) \times \$5,000 / \text{acre} = \$240 / \text{acre}\)  
\((4.8\% - 2003-2007 \text{ avg.})\)
<table>
<thead>
<tr>
<th>Cash Rent Survey</th>
<th>Corn</th>
<th>Soybeans</th>
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<tbody>
<tr>
<td>$200</td>
<td></td>
<td>$200</td>
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<tr>
<td>Per Bushel Yield</td>
<td>$205</td>
<td>$200</td>
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<tr>
<td>Per CSR Point</td>
<td>$200</td>
<td>$200</td>
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<tr>
<td>Gross Income</td>
<td>$363 ($290)</td>
<td>$252 ($202)</td>
</tr>
<tr>
<td>Tenant Residual</td>
<td>$539 ($332)</td>
<td>$311 ($185)</td>
</tr>
<tr>
<td>Crop Share</td>
<td>$355 ($251)</td>
<td>$219 ($156)</td>
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<tr>
<td>Return on Investment</td>
<td>$240</td>
<td>$240</td>
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<tr>
<td>Average</td>
<td>$300 ($245)</td>
<td>$232 ($198)</td>
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</table>

Today’s Average $266 ($222)
2007 Survey Average - $162
Future Consideration

• What are prices (income) going to be?
  – Ethanol impact – how long?
  – Shifts in what is grown – Global impact?

• What are inputs going to cost?
  – Higher oil, higher fertilizer costs.
  – Higher demand for seed, technology cost.
December 2008 Corn Futures
November 2008 Soybean Futures

<table>
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<tr>
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<tr>
<td>7/22/2008</td>
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<td>1250'0</td>
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<td>7/21/2008</td>
<td>1250'0</td>
<td>1225'0</td>
<td>1200'0</td>
<td>1175'0</td>
</tr>
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</table>

May Jun Jul Daily

CME Group
Iowa State University
University Extension
Current ethanol capacity: 141 plants, 8 billion gallons/year

Total capacity under construction and expansion: 5.4 billion gallons/year

59 new ethanol plants and 7 expansion projects underway

2.1 billion bushels of corn were used in producing fuel ethanol in 2006/2007 marketing year.

3.2-3.5 billion bushels of corn are expected to be used in producing fuel ethanol for 2007/2008 marketing year.
U.S. Ethanol Industry

Ethanol Plant Status April 29, 2008
- Currently Not Producing (10)
- Operational (168)
- Planned (320)
- Under-Construction (73)

*Alaska has one ethanol plant in the planning stage
*Hawaii has two ethanol plants in the planning stage
Current biodiesel capacity: 171 plants, 2.24 billion gallons/year

Total capacity under construction and expansion: 1.23 billion gallons/year

60 new plants underway

- 2.8 billion pounds of soybean oil was used in producing biodiesel in 2006/2007 marketing year.

- 3.8 billion pounds of soybean oil are expected to be used in producing biodiesel for 2007/2008 marketing year.
Things to Watch for

• Energy policy changes with the new administration (particularly policy mandates).

• State exemptions to the policy mandate Texas has asked for an exemption – hardship on cattle. Other states are watching.

• Changes in import restrictions, refiner’s credit, etc.
Direct Corn Expenses

- Seed: $36
- Insecticide: $62
- Herbicide: $142

Years: 1997 to 2007
Power Mach Cost vs Invest. Cost
(Per Acre)

Low $96
Mid $76
High $72
Corn Cost of Production – What if?

- Fertilizer: $180
- Seed: $90
- Pesticides: $50
- Insurance: $30
- Machinery: $90
- Drying and storage: $30
- Labor: $30
- Misc: $10
- Interest: $15

Total (w/o rent): $525/180 = $2.92

If Rent $210:
- $735/acre $4.08/bu
- 160 bu (10%) - $4.59
- 120 bu (30%) - $6.13
Bottom Line

• Risk management strategies and tools will be extremely important for 2009.
New Average Crop Revenue Election (ACRE)

• Gives producers a one-time option to choose a revenue-based counter-cyclical payment program, starting in 2009 through 2012

• Producers choose between the current program (LDP and CCP) or ACRE

• Computed on planted acres, up to the total number of base acres on the farm

• Price guarantee is the 2-year average of the national price (seasonal).

Average Crop Revenue Election (ACRE)

- Gives producers a one-time option to choose a revenue-based counter-cyclical payment program, starting in 2009

- Producers choose between the current stable of programs or ACRE

- Producers choosing ACRE agree to 20% decline in direct payments and 30% decline in loan rates
Flexible Cash Leases

Desire:
Stable and predictable rents.

Current Reality:
Prices and yields are very unpredictable.

Potential Solution:
Flexible lease contract
<table>
<thead>
<tr>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>Price and production risk shared as well as profit opportunities</td>
<td>Owner and producer share in risks</td>
</tr>
<tr>
<td>Actual rent adjusts as production or price change</td>
<td>Not as well understood as traditional cash lease or</td>
</tr>
<tr>
<td>Owner does not have to be involved in decision making about inputs or marketing</td>
<td>crop share</td>
</tr>
<tr>
<td></td>
<td>More difficult to calculate</td>
</tr>
<tr>
<td></td>
<td>Owner benefits from tenant’s management skills</td>
</tr>
<tr>
<td></td>
<td>Tenant loses windfall profit potential from high prices</td>
</tr>
</tbody>
</table>
If the final rent does not depend on the farm yield, a flexible rent is still considered to be a cash rent.

Example: base rent on county average yield and actual price at harvest.

County yields are not published until March each year.
Types of Flexible Cash Leases

• Rent varies with both price and yield
  – Matches tenant’s ability to pay
• Rent varies with yield only
  – Could have high yields, low prices
• Rent varies with price, only
  – Could have low yields, high prices
Percent of Cash Rented Acres by Cash Rent Type
or How the Other 10% Live

- Fixed: 90%
- Yield only: 0%
- Price only: 0%
- Yield and Price: 0%
Base plus Bonus

• Paying a “flex bonus” when revenue is above expectations does not affect the split of payments if it is not based on the actual farm yield.

• Provide a copy of your agreement to the FSA county office.
## Flexible Lease Agreement Worksheet

**Ag Decision Maker -- Iowa State University Extension**

For more information, see the information file "Flexible Farm Lease Agreements"

Enter your input values in shaded cells.

### Basic Information
- **Expected acres planted to each crop**
  - Corn: 133 acres
  - Soybeans: 133 acres
- **Base rent-$ per acre (may be zero)**
  - Corn: $130 per acre
  - Soybeans: $130 per acre
- **Base gross revenue-$ per acre (may be zero)**
  - Corn: $463 per acre
  - Soybeans: $322 per acre
- **Share of gross revenue used to calculate rent or bonus-%**
  - 25%
- **USDA loan rate in county (optional)-$ per bushel**
  - Corn: $1.85 per bushel
  - Soybeans: $5.00 per bushel
- **Minimum rent desired (optional)-$ per acre**
  - $150 per acre
- **Maximum rent desired (optional)-$ per acre**
  - $250 per acre

### Expected Yield and Price
- **Expected yield-bushels per acre**
  - Corn: 179 bu. per acre
  - Soybeans: 49 bu. per acre
- **Expected price-$ per bushel**
  - Corn: $5.65 per bushel
  - Soybeans: $11.50 per bushel

### Rent Computation
- **Expected gross revenue under expected yield and price-$/acre**
  - Corn: $1,011.35 per acre
  - Soybeans: $563.50 per acre

### Rent to Pay
- **Rent to pay under expected yield and price-$ per acre**
  - Corn: $250.00 per acre
  - Soybeans: $190.39 per acre

### Average Rent to Pay for Corn and Soybeans-$ per acre
- $220.20 per acre

### Adjusted Average Rent for Corn and Soybeans Combined

| Corn Yield | Soybean Yield | Corn Rent | Soybean Rent | Corn Soybean | Corn Soybean Rent | Corn Soybean Rent | Corn Soybean Rent | Corn Soybean Rent | Corn Soybean Rent | Corn Soybean Rent | Corn Soybean Rent | Corn Soybean Rent | Corn Soybean Rent | Corn Soybean Rent | Corn Soybean Rent | Corn Soybean Rent |
|------------|---------------|-----------|--------------|--------------|------------------|------------------|------------------|------------------|------------------|------------------|------------------|------------------|------------------|------------------|------------------|------------------|------------------|
| 4.00       | 4.25          | 4.50      | 4.75         | 5.00         | 5.25             | 5.50             | 5.75             | 6.00             | 13.00            |
| 10.00      | 10.38         | 10.75     | 11.13        | 11.50        | 11.88            | 12.25            | 12.63            | 13.00            |
| 70.00      | 30.00         | 150       | 150          | 150           | 150              | 150              | 150              | 150              | 150              |
| 90.00      | 35.00         | 150       | 150          | 150           | 150              | 150              | 150              | 150              | 150              |
| 110.00     | 40.00         | 150       | 152          | 154           | 155              | 159              | 165              | 170              | 175              |
| 130.00     | 45.00         | 156       | 161          | 167           | 173              | 179              | 185              | 191              | 198              |
| 150.00     | 50.00         | 171       | 178          | 185           | 192              | 199              | 206              | 213              | 220              |
| 170.00     | 55.00         | 187       | 195          | 203           | 211              | 218              | 226              | 234              | 237              |
| 190.00     | 60.00         | 203       | 212          | 221           | 229              | 236              | 239              | 242              | 244              |
| 210.00     | 65.00         | 219       | 229          | 237           | 240              | 243              | 246              | 249              | 250              |
| 230.00     | 70.00         | 236       | 241          | 244           | 247              | 250              | 250              | 250              | 250              |
### Risk Analysis (optional)

- **Total USDA direct payment for farm:** $5,030 per year
  - **USDA direct payment:** $21.92 per acre
  - **Tenant’s cost of production excluding rent:** $457 per acre
  - **Landowner’s costs for ownership:** $25 per acre
  - **Owner’s share of direct and counter-cyclical payments:** 17%

### Tenant’s Profit for Corn and Soybeans Combined

<table>
<thead>
<tr>
<th>Yield</th>
<th>Corn Yield</th>
<th>Soybean Yield</th>
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</thead>
<tbody>
<tr>
<td>70</td>
<td>$224</td>
<td>$208</td>
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<tr>
<td>90</td>
<td>$159</td>
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<td>110</td>
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<tr>
<td>230</td>
<td>$211</td>
<td>$246</td>
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</tbody>
</table>

### Owner’s Profit for Corn and Soybeans Combined

<table>
<thead>
<tr>
<th>Yield</th>
<th>Corn Yield</th>
<th>Soybean Yield</th>
</tr>
</thead>
<tbody>
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<td>$128</td>
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<td>170</td>
<td>$166</td>
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### Tenant’s Share of Financial Risk: 83%

### Owner’s Share of Financial Risk: 17%
Hazards for 2008 – June 2008

- Economic Profits
- Yields
  - low or at insurance coverage levels due to delayed planting
- Price
  - average or below break even due to CFTC examination of index funds
- Food vs. Fuel debate
  - increased popular press discussion
  - additional ethanol plants coming online
- Farm Bill implementation
- Estate and general tax issues to be addressed with new legislature in 2009
- Decreasing profitability due to rapidly increasing input costs
Other Resources

• Materials from this meeting
  – http://www.extension.iastate.edu/feci/Leasing/vflm.html

• Online Courses – Ag Management e-School
  – http://www.extension.iastate.edu/ames

• Workshops, meetings, conferences
  – http://dbs.extension.iastate.edu/calendar/

• Publications – rental survey, land value survey, etc.
  – http://www.extension.iastate.edu/pubs/

• Articles and spreadsheets
  – http://www.extension.iastate.edu/agdm/

• Private Consultation
  – http://www.extension.iastate.edu/ag/fsfm/fsfarmmg.html
Farm Lease Arrangements

Land Leasing Confidence

- Introduction to Farm Leases
- Cash Rent Leases
- Crop Share Leases
- Custom Farming
- Renting Buildings
- Renting Hay and Pasture Land
- Legal and Tax Considerations
- Conservation and Environmental Considerations
- USDA Agencies and Programs
- Owner and Operator Relations
Farmland Ownership

Purchase Plan

- Land Value Trends
- Using Soils Information
- Appraisal Techniques
- Financing Considerations
- Feasibility of a Land Purchase
Questions…..

Any questions or comments?

Thank You for This Opportunity!

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