

# Fixed and Flexible Cash Rental Arrangements for Your Farm

## Quick Facts for Developing Fixed Cash Rental Rates

### Cash-Rent Market Approach

- Most common way to determine rental rate
- Need knowledge of cash rents being paid for area farms
  - ⇒ Sauk County Average: \$110/acre
- Further adjustments made based on productivity differences and amount and quality of improvements

**Advantage:** Better reflects generalized situations

**Disadvantage:** Difficult to determine cash rents being paid for comparable farms

### Landowner's Ownership Guide

- Calculate resource ownership costs of:
  - ⇒ Land valued at its current fair-market value for agricultural purposes (crop productivity)
    - > Sauk County Average: \$2,500—\$5,000/acre
  - ⇒ Opportunity of interest rate multiplied by land value gives annual land charge
    - Determine the rent-to-value ratio (cash rent divided by market value)
      - > For Wisconsin the rent-to-value ratio is 2-4%
      - Example: For land valued at \$3,500 with a rent-to-value ratio of 3%, the annual land charge would be \$105
      - $$\$3,500 \times 3\% = \$105$$
  - ⇒ Other costs such as investment in land productivity

### Landowner's Adjusted Net-Share Rent

- Assume rent value to be comparable to the net return received under a crop-share lease
- An average net crop share over a period of years should be used to allow for good and bad yields
- Net-Share Rent utilizes: Use production (yield) and price
  - ⇒ Average crop yield and price are available from NASS and FSA, respectively.

**Advantage:** With strong land demand, cash rents may exceed net crop-share rent

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### **Operator's Net Return to Land**

- Requires careful budgeting of: gross crop value, variable and fixed costs, and labor and management costs

**Disadvantage:** Difficulty in determining labor and management values

### **Percent of Land Value**

- Owner looks for a rate of return commensurate with other types of investments, adjusted for differences in risk. Use longer term investments as comparisons.

⇒ For Wisconsin cash rent as a percent of land value is 2-4%

**Disadvantage:** For Owner, there is a potential for land values to decline. For the Operator, there is risk in the variability of yields, market prices, and costs of inputs.

### **Percent of Gross Revenue**

- Cash rental rate is equal to a fixed percent of the expected gross revenue, which sums:
  - ⇒ Income from grain sale or forage production, as well as secondary products (such as straw and stover)
- Expected yield based on actual farm yields from previous years
- Expected prices for major commodities found from:
  - ⇒ Adjusting relevant harvest time futures prices for typical basis values
  - ⇒ Current forward contract prices offered by local buyers at the time
  - ⇒ Crop values are available from FSA

### **Dollars per Bushel of Production**

- Rent is based on fixed value per bushel, based on either the dominant crop applied to all acres or based on all crops produced
- Rental payment value can be based on:
  - ⇒ Expected selling price at the time the rent is negotiated (*Fixed*)
  - ⇒ Current market value of a fixed number of bushels after harvest (*Variable*)

**Advantage:** Reasonable approach when selling prices are relatively stable

## Quick Facts for Flexible Cash-Rent Arrangements

### Flexing for Crop Price Only

1. Base rent multiplied by ratio of current year's price to base price
2. Rent equal to the value of a fixed amount of commodity
3. Base rent with stated adjustments for prices outside a specified range
4. Minimum base rent with upward adjustments

**Advantage:** Landowner shared in additional income from increase in crop price

**Disadvantage:** Increase risk substantially for Operators. A short crop leads to higher prices and rent.

### Flexing for Yield Only

- For consideration when crop yields are highly uncertain and crops are grown for livestock feed, with no relevant market price
1. Rent is equal to base rent multiplied by ratio of actual yield to base yield,
    - ⇒ Base yield is equal to long-term average or expected yield
  2. Actual yield multiplied by fixed dollar value per bushel or ton
    - Land valued at its current fair-market value for agricultural purposes (crop)
- Important to specify standard quality grade and/or moisture level

**Disadvantage:** More Landowner concern over accuracy of reported yields

### Flexing for Crop Price and Yield

- Operator and Landowner agree on base cash rent tied to a base yield and a base expected price for each crop being considered
- Yield change adjustments should be based on yields actually obtained from farm

### Flexing Rent on Changes in Cost of Inputs

- Stabilize bottom line for operators by factoring in ratio of base year's cost of inputs to the current year's cost of inputs
  - ⇒ Consider: seed, fertilizer, pesticides, and diesel and drying fuel