

## Crop Rental Arrangements. . .

In a new risk era

Kevin C. Dhuyvetter, K-State Ag. Economist  
 Terry L. Kastens, K-State Ag. Economist  
 kcd@ksu.edu – 785-532-3527  
 tkastens@ksu.edu – 785-626-9000

www.agmanager.info

Presented at:  
 2008 Agricultural Lenders Conference  
 October 1, 2008; Garden City, Kansas  
 October 8, 2008; Manhattan, Kansas



1

## Basic Lease Types

- **Crop-share**
  - Landowner shares in annual revenues and typically in certain annual costs
- **Cash rent**
  - Landowner gets a fixed annual cash amount for use of land
- **Numerous variants around these two**

2

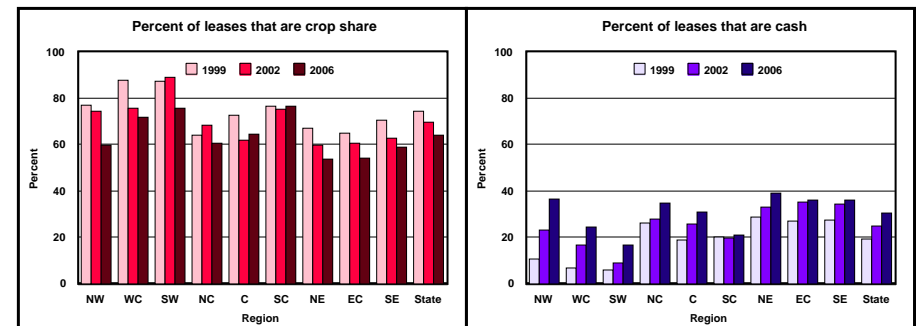
## Distribution of leases by type of lease ...

Region	Cash	Share	Other
Northwest	36.3%	59.8%	3.9%
West Central	24.3	71.7	4.0
Southwest	16.5	75.5	8.0
North Central	34.9	60.5	4.6
Central	30.9	64.6	4.5
South Central	21.0	76.4	2.6
Northeast	38.8	53.5	7.7
East Central	36.0	54.3	9.6
Southeast	36.2	58.9	4.9
State	30.5	63.9	5.6

Source: Schlegel and Tsoodle -- 2006 KAS/KSU survey

3

## Basic Lease Types in Kansas



Source: KSU and KS Ag Stat – Non-Irrigated Farm Lease Arrangement Surveys

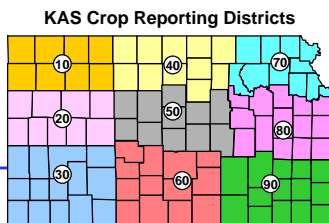
**Crop share continues to be the most prevalent, but the trend has been a shift from crop share arrangements towards more cash rent leases.**

### Questions to ask:

- 1) What factors have been behind this trend?
- 2) Do we expect this to continue or to reverse in current environment?

4

## Length of cropland leases ...



Region	Years rented
Northwest (10)	17.6
West Central (20)	21.0
Southwest (30)	20.0
North Central (40)	16.9
Central (50)	17.2
South Central (60)	15.5
Northeast (70)	17.2
East Central (80)	18.8
Southeast (90)	15.6
<b>State</b>	<b>17.8</b>

Source: Schegel and Tsoodle -- 2006 KAS/KSU survey

5

## In recent years, the majority of leasing questions received pertain to:

- Impact of adopting new technologies
- Cash renting
- “Non-traditional” leases
  - Net share rent
  - Flexible cash rent
  - Bushel rent
  - Combination cash/cropshare

... while current “hot topic” is slightly different, method of addressing questions has not changed.

6

## Determining the terms of a crop lease ...

- How are cash lease rates or the terms of crop share leases established?
  - Short answer is “the market”
- While landowners and tenants (i.e., the market) ultimately determine terms of crop share and cash leases, we use the equitable concept to arrive at a starting point for negotiations – and to better understand the market.

7

## Equitable vs. traditional share rent ...

**Equitable:** Income is shared in the same proportion as the contribution of total inputs.

**Traditional:** Income and shared expenses (if any) are shared in the same proportion as what has been done in the past. Share rent based on tradition may, or may not, be equitable.

**Traditional = Equitable in the long-run**

## KSU-Lease.xls

- A what-if spreadsheet to analyze rents
- Delineates relative contributions
- Allows considering cash vs. crop-share
  - Can deal with a risk premium
- Very flexible; can handle
  - Net share leases
  - Fixed bushel rents
  - Cash transfers
- Important purpose is to allow people to move beyond traditional leases when they need to change (and to analyze impact of cash rent)

9

## A good crop share lease should follow five basic principles ...

1. Yield increasing inputs should be shared
  2. Share arrangements should be reviewed as technology changes
  3. Total returns divided in same proportion as resources contributed
- 
4. Compensation for unused long-term investments at termination
  5. Good landlord/tenant communications

10

**Principle #3:**  
Returns divided in same proportion as resources contributed.

This requires annual contributions of both parties to be identified (budgeting type approach).



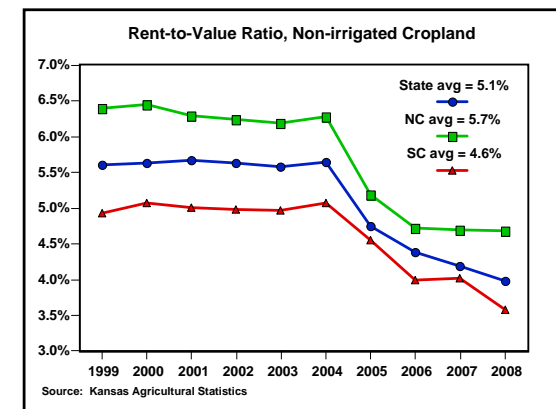
Base input values on expectations consistent with the time-frame of the lease (if expectations end up being significantly off, be willing to make adjustments).

11

## Land contribution ...

The land contribution has typically been based on an “average market value” for the land along with an historical average return to land.

As cash leases become more common, the land contribution can be set equal to the cash rent.



12

## Machinery contributions ...

Machinery contribution should be based on average costs. Two methods for estimating the machinery contribution:

1. Machinery investment approach - annual contribution is based on depreciation, interest, repairs, fuel and oil, and labor.
2. Custom rates approach - annual contribution is based on reported custom rates and the typical operations.



13

## Crop production input contributions ...

The value of contributions for input expenses such as seed, herbicides, insecticides, fertilizer, etc. are generally valued at current market prices and represent “typical” production practices.

How do we deal with input prices if they currently deviate significantly from historical averages (e.g., fertilizer, fuel)?

We'll come back to this again

14

## Tests of a good crop share lease ...

- Are yield increasing inputs shared?
- Does it have flexibility to deal with change?
- Does it promote optimal management?
- Is income shared in same % as contributions?
- Is it written?
- Will it be reviewed periodically?
  - Keep the automatic rollover clauses out!
- Do all parties agree that lease is “fair”?

15

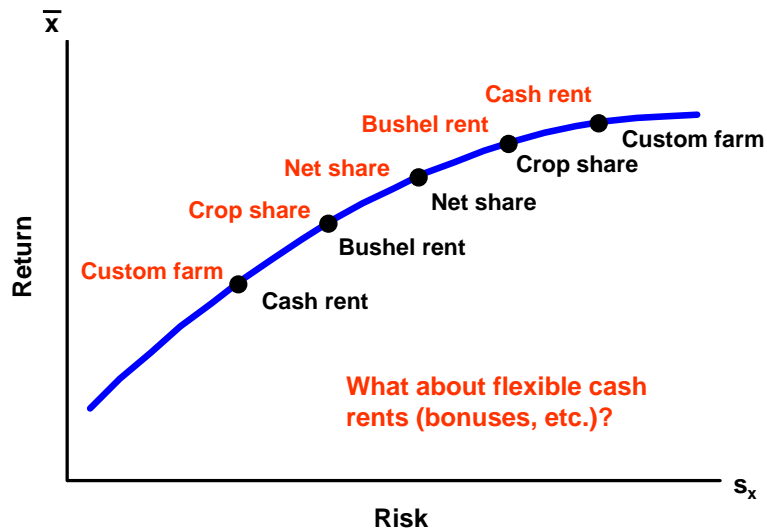
## “Non-traditional” leases ...

- Cash rent
- Net share rent
- Bushel rent
- Flexible cash rent
- Combination cash and crop share rent

Because there is currently much interest in these types of leases, there must be good reasons to use them ...

16

## Landowner/producer risk-return tradeoff



17

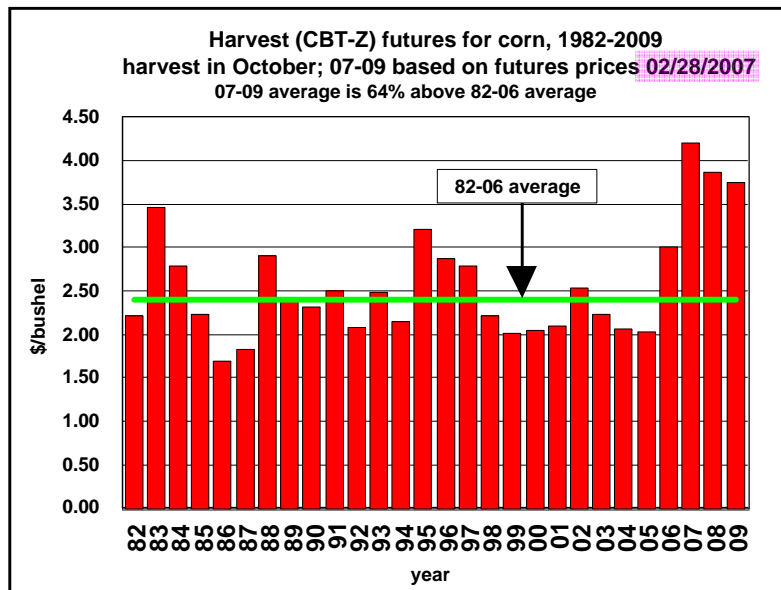
## Risk

- Risk: variation about expected outcome
  - Suggests that the cash-equivalent of a share lease will be greater than cash rent
- Hasn't helped much in understanding rents
  - Tenant's risk lower recently (1990s thru 2006)
  - Cash rent is not riskless
  - Costs may be higher with share rents
    - So cash rents may be higher than share rents i.e., tenants bid up cash rents to avoid costs
- Crop share rent shares are sticky
  - Only way to bid up rents is through cash rent

Just when we got used to ignoring risk, it seems to come back into play . . .

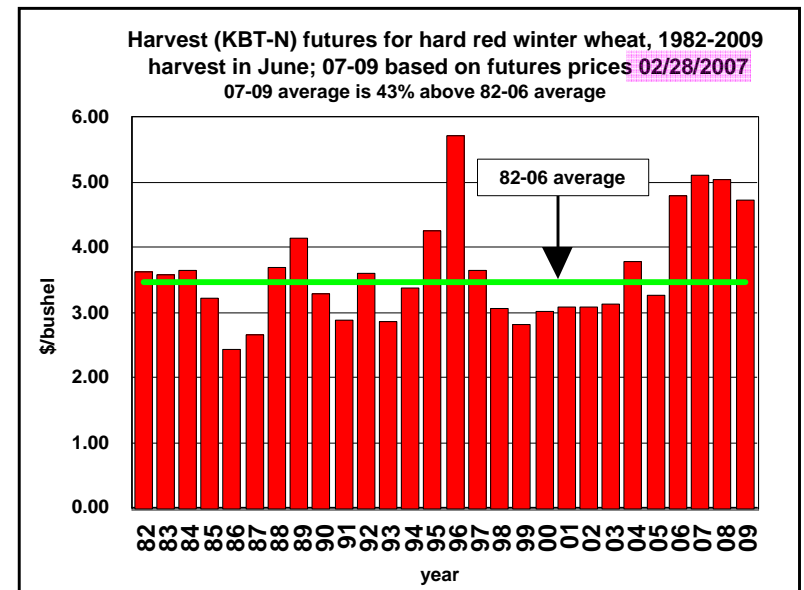
18

## In late 06/early 07 the crop price world changed!



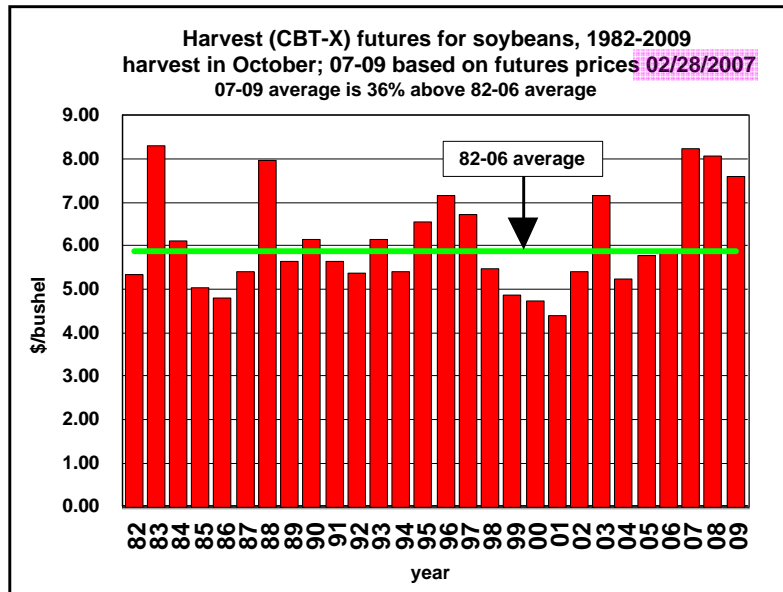
19

## It's not just corn!



20

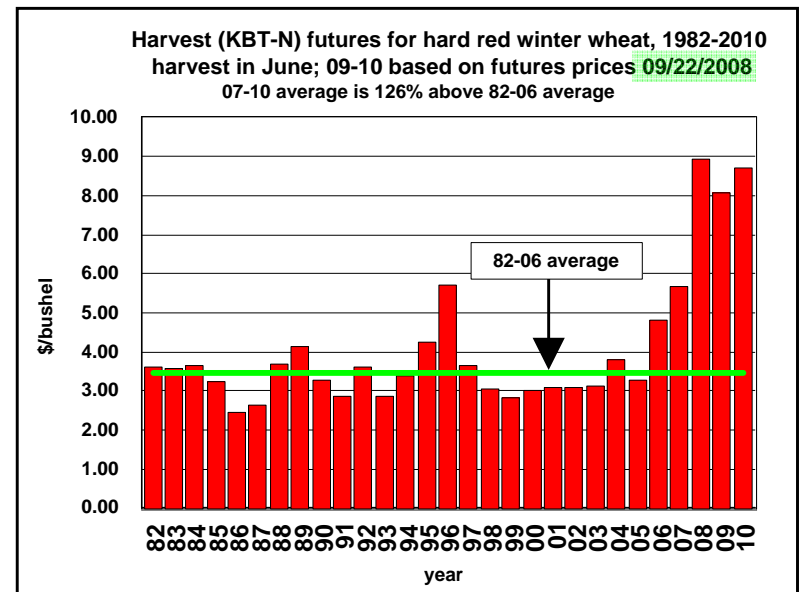
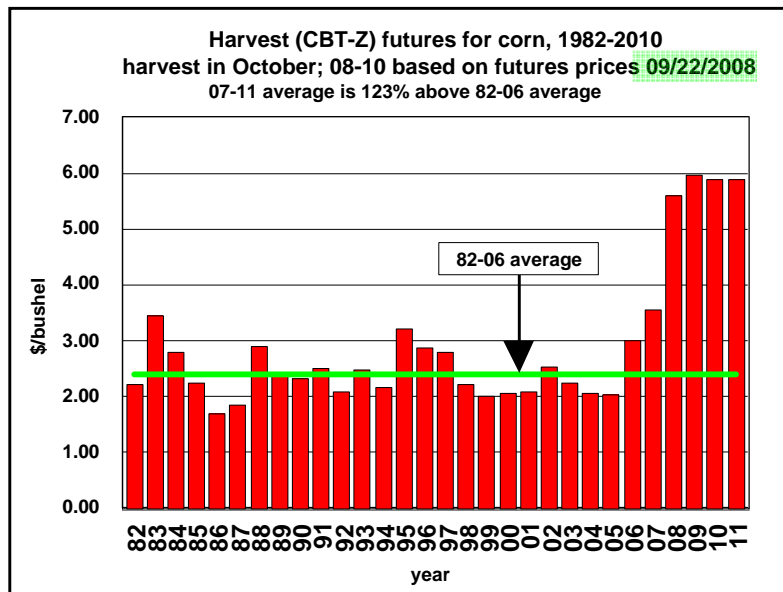
It's not just corn!

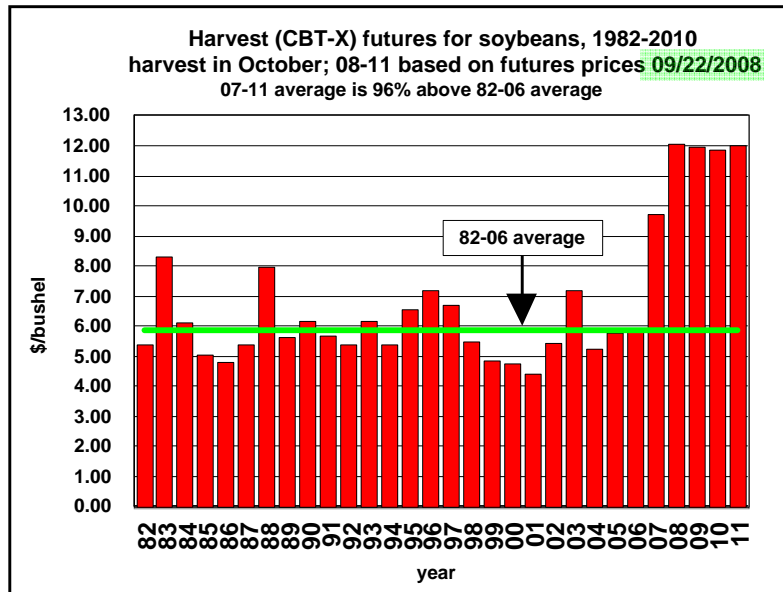


The "new world" (started in 07)

- Landlords detected massive profits
  - Using 3-year expectations, tenants "could" pay as much as 2x-3x of going market rental rates
- Land prices rise
- Cash rents not keeping up
  - Risk? Poor information? Taking advantage?
  - Some landowners wish to go back to crop-share
- Some tenants jumping cash rents
- Some tenants paying bonus rents
  - What are the FSA issues
  - Will bonuses be expected in future?

And, expected crop prices are even better today!





It's not surprising that landowners are revisiting leasing arrangements!

25

## Flexible cash rents (method of paying bonuses)

### 1) Establish base cash rent

### 2) Flex/modify base rent based on...

- price deviation from base (fixed bushel rent)
- yield deviation from base
- price and yield (revenue) deviation from base

#### • Does flex work both ways?

- Communication and documentation are extremely important to make sure everybody understands what they are agreeing to

26

#### Example of Flex Lease

Base cash rent, \$/acre	\$60.00
Flex direction (Both (up and down) vs Up)	Up
Percent of change to factor into flexible rent	50.0%

	Wheat	Sorghum	Soybeans	
Base acres	80	50	30	160
Base yield	45	80	30.00	
Base price	\$5.50	\$5.00	\$10.00	
Revenue	\$247.50	\$400.00	\$300.00	\$48,800

#### Issues to resolve:

- 1) Where does base cash rent come from?
- 2) Where do base acres, yields, and prices come from (these should be consistent with base rent)?
- 3) Does rent flex on yield, price, or combination (revenue)?
- 4) Does rent flex both directions or only up?
- 5) What percent change from base should be used?

27

#### Example of Flex Lease

Base cash rent, \$/acre	\$60.00
Flex direction (Both (up and down) vs Up)	Up
Percent of change to factor into flexible rent	50.0%

	Wheat	Sorghum	Soybeans		% chg from base
Base acres	80	50	30	160	
Base yield	45	80	30.00		
Base price	\$5.50	\$5.00	\$10.00		
Revenue	\$247.50	\$400.00	\$300.00	\$48,800	
Actual acres	75	48	37	160	
Actual yield	41	73	28	\$44,793	-8.2%
Actual price	\$7.80	\$5.25	\$12.75	\$60,638	24.3%
Revenue	\$319.80	\$383.25	\$357.00	\$55,590	13.9%

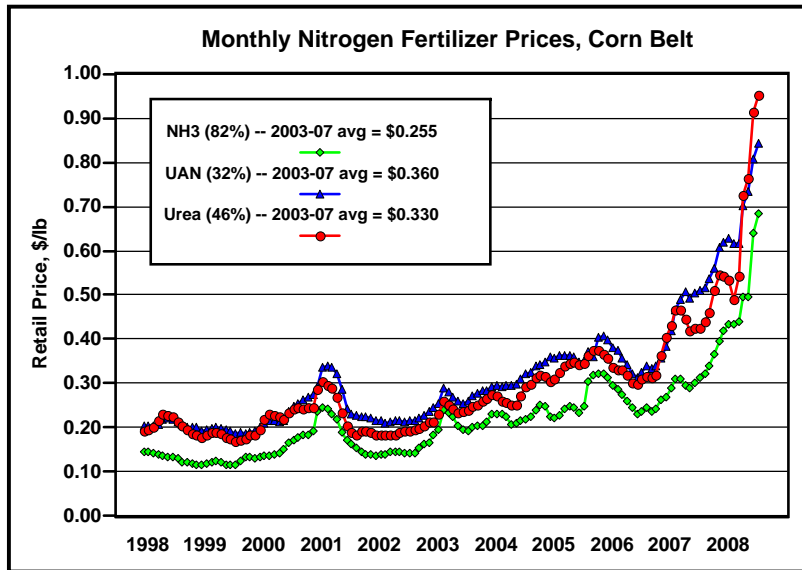
Cash rent flexing on yield only	\$60.00
Cash rent flexing on price only	\$67.28
Cash rent flexing on revenue (yield and price)	\$64.17

#### Issues to resolve:

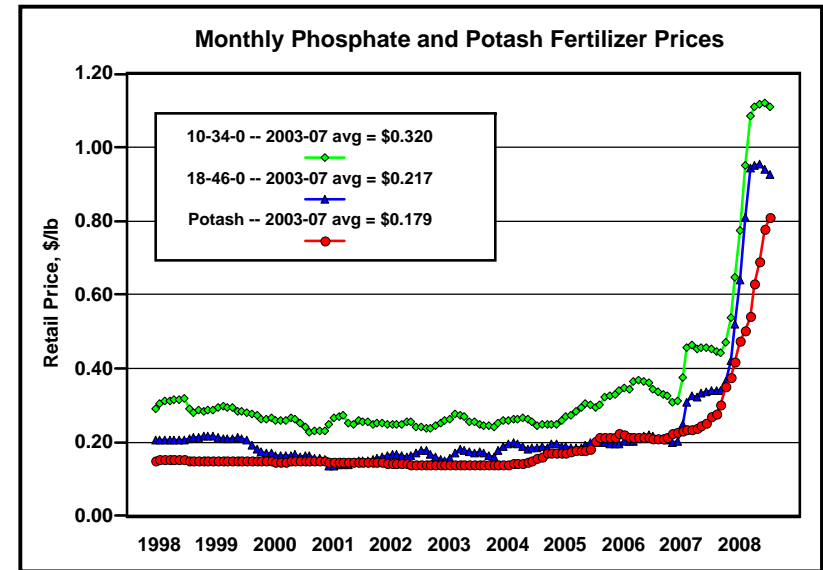
- 1) Do you use actual acres or base acres in calculations?
- 2) Do you use actual yields or county yields (do they need to be verified)?
- 3) What actual prices should be used (location, time, etc)?

28

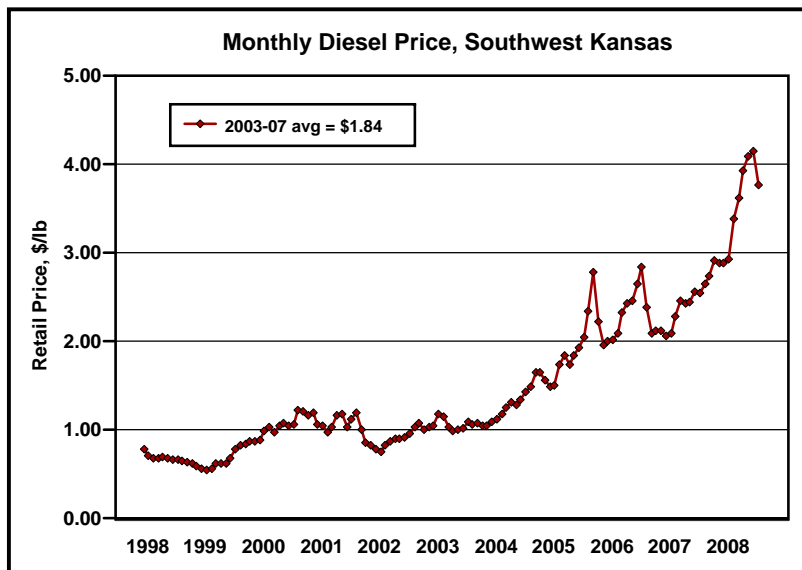
Input prices jumped up a little later than crop prices



29



30



31

The “newer” new world

- Fertilizer, herbicide, machinery costs, and fuel, all have taken massive jumps in the last 12 months
  - Availability sometimes bigger worry than price
  
- Tenant’s risk has greatly increased
  - Less of a problem in crop share leases
  
- Expected crop prices still swamp input prices but a very large risk premium remains between crop-share and cash rent terms
  - Makes it difficult to determine whether the terms we observe are appropriate or inappropriate

32

## 2009 KSU Farm Management Guides for South Central KS

(prices are average of 2009 forecasts and 2009-2013 forecasts)

### CROP BUDGETS SHOWING TOTAL COSTS AND RETURNS

Crop/System	Corn	Milo	Soybeans	Wheat-R	Wheat-C	DC SB	Total	Per	Per
Planted acres of each crop	10.0	50.0	20.0	80.0	160.0	0.0	320.0	Acres	Acres
Tillable acres per planted acre	1.0	1.0	1.0	1.0	1.0	0.0	320.0	Planted	Tillable
<b>INCOME PER ACRE</b>									
A. Yield per acre	90.0	80.0	27.0	45.0	45.0	20.0	---	---	---
B. Price per unit	\$5.00	\$4.90	\$10.73	\$7.19	\$7.19	\$10.73	---	---	---
C. Net government payments	\$15.35	\$15.35	\$15.35	\$15.35	\$15.35	\$0.00	\$4,912	\$15.35	\$15.35
D. Indemnity payments	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0	\$0.00	\$0.00
E. Miscellaneous income	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0	\$0.00	\$0.00
F. Returns/acre ((A x B) + C + D + E)	\$465.35	\$407.35	\$304.93	\$338.68	\$338.68	\$214.50	\$112,402	\$351.25	\$351.25
<b>COSTS PER ACRE</b>									
1. Seed	\$47.04	\$9.48	\$33.75	\$19.00	\$11.40	\$40.00	\$4,963	\$15.51	\$15.51
2. Herbicide	26.19	20.03	17.12	2.85	6.43	18.90	2,862	8.94	8.94
3. Insecticide / Fungicide	1.00	0.00	0.00	1.00	1.00	0.00	250	0.78	0.78
4. Fertilizer and Lime	113.53	100.88	31.16	105.90	81.48	21.80	28,311	88.47	88.47
5. Crop Consulting	0.00	0.00	0.00	0.00	0.00	0.00	0	0.00	0.00
6. Crop Insurance	0.00	0.00	0.00	0.00	0.00	0.00	0	0.00	0.00
7. Drying	0.00	0.00	0.00	0.00	0.00	0.00	0	0.00	0.00
8. Miscellaneous	5.75	5.75	5.75	5.75	5.75	5.75	1,840	5.75	5.75
9. Machinery Expense	101.72	91.49	54.72	98.87	98.87	53.57	30,414	95.04	95.04
10. Non-machinery Labor	11.44	10.40	6.24	11.18	11.18	6.11	3,442	10.76	10.76
11. Irrigation	0.00	0.00	0.00	0.00	0.00	0.00	0	0.00	0.00
12. Land Charge / Rent	46.00	46.00	46.00	46.00	46.00	0.00	14,720	46.00	46.00
G. SUB TOTAL	\$352.67	\$284.03	\$194.74	\$290.54	\$262.10	\$146.13	\$86,803	\$271.26	\$271.26
13. Interest on 1/2 Nonland Costs	10.90	8.30	5.22	8.46	7.32	5.13	2,476	7.74	7.74
H. TOTAL COSTS	\$363.58	\$292.32	\$199.95	\$299.00	\$269.42	\$151.26	\$89,279	\$279.00	\$279.00
I. RETURNS OVER COSTS (F - H)	\$101.77	\$115.03	\$104.97	\$39.67	\$69.25	\$63.24	\$23,123	\$72.26	\$72.26
J. TOTAL COSTS/UNIT (H/A)	\$4.04	\$3.65	\$7.41	\$6.64	\$5.99	\$7.56	---	---	---
K. RETURN TO TOTAL COST ((I+13)/G)	31.95%	43.42%	56.58%	16.57%	29.21%	46.79%	25.90%	25.90%	25.90%

Equitable crop share arrangement is 70.3 / 29.7 with landowner sharing fertilizer, herbicides, insecticides, and chemical applications (except NH3). But, is land charge/rent high enough?

33

## 2009 KSU Farm Management Guides for South Central KS

(prices are average of 2009 forecasts and 2009-2013 forecasts)

### CROP BUDGETS SHOWING TOTAL COSTS AND RETURNS

Crop/System	Corn	Milo	Soybeans	Wheat-R	Wheat-C	DC SB	Total	Per	Per
Planted acres of each crop	10.0	50.0	20.0	80.0	160.0	0.0	320.0	Acres	Acres
Tillable acres per planted acre	1.0	1.0	1.0	1.0	1.0	0.0	320.0	Planted	Tillable
<b>INCOME PER ACRE</b>									
A. Yield per acre	90.0	80.0	27.0	45.0	45.0	20.0	---	---	---
B. Price per unit	\$5.00	\$4.90	\$10.73	\$7.19	\$7.19	\$10.73	---	---	---
C. Net government payments	\$15.35	\$15.35	\$15.35	\$15.35	\$15.35	\$0.00	\$4,912	\$15.35	\$15.35
D. Indemnity payments	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0	\$0.00	\$0.00
E. Miscellaneous income	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0	\$0.00	\$0.00
F. Returns/acre ((A x B) + C + D + E)	\$465.35	\$407.35	\$304.93	\$338.68	\$338.68	\$214.50	\$112,402	\$351.25	\$351.25
<b>COSTS PER ACRE</b>									
1. Seed	\$47.04	\$9.48	\$33.75	\$19.00	\$11.40	\$40.00	\$4,963	\$15.51	\$15.51
2. Herbicide	26.19	20.03	17.12	2.85	6.43	18.90	2,862	8.94	8.94
3. Insecticide / Fungicide	1.00	0.00	0.00	1.00	1.00	0.00	250	0.78	0.78
4. Fertilizer and Lime	113.53	100.88	31.16	105.90	81.48	21.80	28,311	88.47	88.47
5. Crop Consulting	0.00	0.00	0.00	0.00	0.00	0.00	0	0.00	0.00
6. Crop Insurance	0.00	0.00	0.00	0.00	0.00	0.00	0	0.00	0.00
7. Drying	0.00	0.00	0.00	0.00	0.00	0.00	0	0.00	0.00
8. Miscellaneous	5.75	5.75	5.75	5.75	5.75	5.75	1,840	5.75	5.75
9. Machinery Expense	101.72	91.49	54.72	98.87	98.87	53.57	30,414	95.04	95.04
10. Non-machinery Labor	11.44	10.40	6.24	11.18	11.18	6.11	3,442	10.76	10.76
11. Irrigation	0.00	0.00	0.00	0.00	0.00	0.00	0	0.00	0.00
12. Land Charge / Rent	46.00	46.00	46.00	46.00	46.00	0.00	14,720	46.00	46.00
G. SUB TOTAL	\$352.67	\$284.03	\$194.74	\$290.54	\$262.10	\$146.13	\$86,803	\$271.26	\$271.26
13. Interest on 1/2 Nonland Costs	10.90	8.30	5.22	8.46	7.32	5.13	2,476	7.74	7.74
H. TOTAL COSTS	\$363.58	\$292.32	\$199.95	\$299.00	\$269.42	\$151.26	\$89,279	\$279.00	\$279.00
I. RETURNS OVER COSTS (F - H)	\$101.77	\$115.03	\$104.97	\$39.67	\$69.25	\$63.24	\$23,123	\$72.26	\$72.26
J. TOTAL COSTS/UNIT (H/A)	\$4.04	\$3.65	\$7.41	\$6.64	\$5.99	\$7.56	---	---	---
K. RETURN TO TOTAL COST ((I+13)/G)	31.95%	43.42%	56.58%	16.57%	29.21%	46.79%	25.90%	25.90%	25.90%

Land charge is 10% increase from 2008 cash rents.

Equitable crop share arrangement is 70.3 / 29.7 with landowner sharing fertilizer, herbicides, insecticides, and chemical applications (except NH3). But, is land charge/rent high enough?

34

## 2009 KSU Farm Management Guides for South Central KS

(prices are average of 2009 forecasts and 2009-2013 forecasts)

### ALTERNATIVE METHODS OF ESTIMATING CASH RENT

7:11 AM 09/26/08

Crop/System	Corn	Milo	Soybeans	Wheat-R	Wheat-C	DC SB	Total	Per	Per
Total tillable acre	10.0	50.0	20.0	80.0	160.0	0.0	320.0	Planted	Tillable
Planted acres of each crop	10.0	50.0	20.0	80.0	160.0	0.0	320.0	Planted	Tillable
<b>A. Landowner's COST</b>									
Land	\$46.00	\$46.00	\$46.00	\$46.00	\$46.00	\$0.00	\$14,720	\$46.00	\$46.00
Irrigation equipment	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0	\$0.00	\$0.00
Total	\$46.00	\$46.00	\$46.00	\$46.00	\$46.00	\$0.00	\$14,720	\$46.00	\$46.00
<b>B. Landowner's EQUITABLE SHARE RENT ---- risk adj factor</b>									
Total income	\$465.35	\$407.35	\$304.93	\$338.68	\$338.68	\$214.50	\$112,402	\$351.25	\$351.25
Landowner's share	29.7%	29.7%	29.7%	29.7%	29.7%	29.7%	29.7%	29.7%	29.7%
Landowner's income	\$138.05	\$120.84	\$90.46	\$100.47	\$100.47	\$63.63	\$33,345	\$104.20	\$104.20
Landowner operating expense	49.79	44.10	21.69	40.24	33.81	11.765	11,765	36.77	36.77
Income less operating expense	\$88.25	\$76.75	\$68.77	\$60.23	\$66.66	\$47.94	\$21,579	\$67.44	\$67.44
Less risk adjustment	0.00	0.00	0.00	0.00	0.00	0.00	0	0.00	0.00
Cash rent equivalent	\$88.25	\$76.75	\$68.77	\$60.23	\$66.66	\$47.94	\$21,579	\$67.44	\$67.44
<b>C. Amount tenant CAN AFFORD TO PAY</b>									
Total income	\$465.35	\$407.35	\$304.93	\$338.68	\$338.68	\$214.50	\$112,402	\$351.25	\$351.25
Total operating expense	\$317.58	\$246.32	\$153.95	\$253.00	\$223.42	\$151.26	\$74,559	\$233.00	\$233.00
Return to land and irr equip	\$147.77	\$161.03	\$150.97	\$85.67	\$115.25	\$63.24	\$37,843	\$118.26	\$118.26
<b>Comparison of alternative cash rent methods</b>									
Low	\$46.00	\$46.00	\$46.00	\$46.00	\$46.00	\$0.00	\$14,720	\$46.00	\$46.00
Average	\$94.01	\$94.59	\$88.58	\$63.97	\$75.97	\$37.06	\$24,714	\$77.23	\$77.23
High	\$147.77	\$161.03	\$150.97	\$85.67	\$115.25	\$63.24	\$37,843	\$118.26	\$118.26
Returns above all costs (profit)	\$101.77	\$115.03	\$104.97	\$39.67	\$69.25	\$63.24	\$23,123	\$72.26	\$72.26

If risk premium = 0%, landowner would be considerably better off with equitable crop share arrangement compared to cash rent.

35

## 2009 KSU Farm Management Guides for South Central KS

(prices are average of 2009 forecasts and 2009-2013 forecasts)

### ALTERNATIVE METHODS OF ESTIMATING CASH RENT

7:13 AM 09/26/08

Crop/System	Corn	Milo	Soybeans	Wheat-R	Wheat-C	DC SB	Total	Per	Per
Total tillable acre	10.0	50.0	20.0	80.0	160.0	0.0	320.0	Planted	Tillable
Planted acres of each crop	10.0	50.0	20.0	80.0	160.0	0.0	320.0	Planted	Tillable
<b>A. Landowner's COST</b>									
Land	\$46.00	\$46.00	\$46.00	\$46.00	\$46.00	\$0.00	\$14,720	\$46.00	\$46.00
Irrigation equipment	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0	\$0.00	\$0.00
Total	\$46.00	\$46.00	\$46.00	\$46.00	\$46.00	\$0.00	\$14,720	\$46.00	\$46.00
<b>B. Landowner's EQUITABLE SHARE RENT ---- risk adj factor</b>									
Total income	\$465.35	\$407.35	\$304.93	\$338.68	\$338.68	\$214.50	\$112,402	\$351.25	\$351.25
Landowner's share	29.7%	29.7%	29.7%	29.7%	29.7%	29.7%	29.7%	29.7%	29.7%
Landowner's income	\$138.05	\$120.84	\$90.46	\$100.47	\$100.47	\$63.63	\$33,345	\$104.20	\$104.20
Landowner operating expense	49.79	44.10	21.69	40.24	33.81	11.765	11,765	36.77	36.77
Income less operating expense	\$88.25	\$76.75	\$68.77	\$60.23	\$66.66	\$47.94	\$21,579	\$67.44	\$67.44
Less risk adjustment	28.05	24.39	21.85	19.14	21.18	15.24	6,858	21.43	21.43
Cash rent equivalent	\$60.21	\$52.36	\$46.91	\$41.09	\$45.48	\$32.70	\$14,722	\$46.00	\$46.00
<b>C. Amount tenant CAN AFFORD TO PAY</b>									
Total income	\$465.35	\$407.35	\$304.93	\$338.68	\$338.68	\$214.50	\$112,402	\$351.25	\$351.25
Total operating expense	\$317.58	\$246.32	\$153.95	\$253.00	\$223.42	\$151.26	\$74,559	\$233.00	\$233.00
Return to land and irr equip	\$147.77	\$161.03	\$150.97	\$85.67	\$115.25	\$63.24	\$37,843	\$118.26	\$118.26
<b>Comparison of alternative cash rent methods</b>									
Low	\$46.00	\$46.00	\$46.00	\$41.09	\$45.48	\$0.00	\$14,720	\$46.00	\$46.00
Average	\$84.66	\$86.46	\$81.29	\$57.59	\$68.91	\$31.98	\$22,428	\$70.09	\$70.09
High	\$147.77	\$161.03	\$150.97	\$85.67	\$115.25	\$63.24	\$37,843	\$118.26	\$118.26
Returns above all costs (profit)	\$101.77	\$115.03	\$104.97	\$39.67	\$69.25	\$63.24	\$23,123	\$72.26	\$72.26

At a risk premium of roughly 32%, landowner would be indifferent between fixed cash rent and equitable crop share leases.

36



## Cash rents rise over time

- Although cash rents do fall about 30% of the years, on average they rise 2-3% annually
  - Unusual to see a 3-year contract rate that shouldn't be higher than the previous contract
- Landowners & tenants who see stable crop-share terms for years think that translates to stable cash rent
  - We see cash rental rates that haven't changed for years and decades
    - Landlord: "We didn't know."
    - Tenant: "She never asked for a higher rent."

41

## Manna-from-heaven payments

- Unexpected payments, typically from the government, should be shared according to parties' costs
  - Examples: CRP, CSP, EQIP
- If tenant does nothing to earn payment it should go to the land, i.e., the landowner
- Such payments should be discussed between landowner & tenant (especially the relative associated costs)

42

## Foot-in-door high rental payments

- High rent payments on new contracts often are followed by stagnant rates for many years, which could be:
  - A) Tenant overbids to get land, then realizes he's not profitable so rationalizes stagnant rents
  - B) Tenant uses this as a strategy to acquire land and pay lower-than-market rents over time
    - This is the least ethical outcome of the two
- Some tenants who do this actually beg for lower rents in near future, realizing that landlords are reluctant to change tenants
  - This is really unethical!

43

## Landowners need money too

- Tenants often make the argument that "she doesn't need the money"
  - This is completely irrelevant!
- Admittedly, landowners sometimes foster this perception
  - . . . which tends to change when investment-minded heirs acquire land being rented

44

## Landowner ethics

- Landowners may use their land for non-ag purposes and yet expect the same rent
  - Utility poles, oil leases
  - Lease hunting
- Landowners think if they paid too much for land it should bring a higher rent
  - This is completely irrelevant!
- Landowners might demand certain farming practices yet expect market rent
  - e.g., no fertilizer; conventional tillage
- Landowners make demands on current tenants to “fix” problems of past tenants

45

## Family situations often are the worst

- “Sweat-equity” parent-child relationships lead to unrealistic expectations across generations
- Family members have trouble believing their own parents, children, or siblings would cheat them
  - Backlash then goes overboard
- Family members often are “always around” and so the pain always resurfaces
  - Hard to “forget and move on”

46

## Ethics is good long run economics

- Poor ethics results in high tenant turnover:
  - Increases cost of relationship establishment and monitoring
  - Reduces profit to the land (tenant makes short run decisions)
- Bad business leads to unethical behavior
  - Poor management causes “I deserve more”
  - Bad behavior is rationalized
- Good ethics should emerge because it is the “right thing to do,” not for the purpose of long-run profit-maximization

47

## Miscellaneous

- Landowners rarely will evict tenants!
  - Often will sell land rather than evict tenants
  - Will put up with atrocious behavior of tenants (especially relatives)
- Attorneys have some blame
  - Promote perceptions of “poor returns to farming,” “sweat equity,” etc.
  - Believe, like many, that farming is “special”
- Attorneys should
  - Tell landowners it’s okay to evict tenants
  - Help clients understand that FARMING IS A BUSINESS!

48

## What does this all mean for lenders?

- Don't be among those condoning bad rental ethics/economics
- Borrowers are going to need a lot of money
- The boom is NOT over!

49

## Questions ???



[www.agmanager.info](http://www.agmanager.info)



50