

Fixed and Flexible Cash Rental Arrangements

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September 2011

NDSU
Extension Service

Fixed Cash Rent Methods

1. Cash rent market approach
2. Landowner's cost or desired return
3. Landowner's adjusted net-share rent
4. Operator's net return to land
5. Percent of land value
6. Percent of gross revenue
7. Dollars per bushel of production
8. Fixed bushel rent

Other Options to Determine Fixed Cash Rent

1. Bid process
2. Auction process
3. Professional farm manager

Putting Flexibility in Cash Rent Agreements

1. Crop-share leases were the original flexible rents
 1. The scale of today's operation makes share rents impractical
2. Cash rents may be adjusted by market prices, crop yields and production costs

Advantages of Flexible Cash Rents

1. Landowner shares in additional income from:
 1. Price increase
 2. Yield increase
2. Reduced risk for operator when:
 1. Prices drop
 2. Yields are reduced

Disadvantages of Flexible Cash Rents

1. Increased risk for landowner
2. Landowner may be concerned about accuracy of reported yields
3. Higher rent due to increased yields means the operator may be giving up some of the benefit from managerial input
4. Calculating the rent requires more management and communication

Methods of Flexing Cash Rent

Flexing for Crop Price Only

Increases risk substantially for operators

Example 1.

Base rent multiplied by ratio of current years price to base price.

Base rent x (current years price ÷ base price) = current years rent.

$$\$60 \times (\$12.00 \div \$10.00) = \$72$$

Flexing for Crop Price Only

Example 2.

Rent equal to the value of a fixed amount of commodity.

“The amount of cash rent is equal to the value 8 bushels of soybeans based on the average daily closing price for the month of November.”

$$8 \text{ bushels} \times \$12.00 = \$96.00$$

Flexing for Crop Price Only

Example 3.

Base rent with stated adjustments for prices outside a specified range.

Owner and operator agree on a rent of \$60 per acre if the current price of soybeans is between \$9.00 and \$10.00 per bushel. For each \$0.50 change in price above or below this range the rent will increase or decrease by \$5.00 per acre.

Flexing for Crop Price Only

Example 4.

Minimum base rent with upward adjustments.

Owner and operator agree to a base rent of \$50.00 per acre if the soybean price is \$9 per bushel or less. For each \$0.50 per bushel increase the rent will increase \$5.00 per acre.

Flexing for Yield Only

Example 1.

Base rent is multiplied by a ratio of the current yield divided by a base yield to calculate current rent

$$\$60 \times (35 \text{ bu} \div 40 \text{ bu}) = \$52.50$$

Flexing for Yield Only

Example 2.

Actual yield is multiplied by a fixed value per bushel decided in advance.

Rent equals actual yield times \$2.00 per bushel for wheat.

$$35 \text{ bu yield} \times \$2.00 = \$70 \text{ per acre}$$

Flexing for Price and Yield

Example 1.

Operator and landowner agree to a base cash rent tied to a base yield and a base price.

Base rent x (current yield ÷ base yield) x (current price ÷ base price)

$$\$60 \times (45 \text{ bu} \div 40 \text{ bu}) \times (\$6.50 \div \$7.00) = \$62.68$$

Flexing for Price and Yield

Example 2.

Rent equals an agreed upon percentage of crop value

$$42 \text{ bu} \times \$6.50 \times 25\% = \$68.25$$

Flexing for Price and Yield

Example 3.

Minimum base rent plus a bonus

Rent equals \$60 plus 30% of total revenue per acre above \$225.00 per acre

$$40 \text{ bu} \times \$7.00 = \$280$$

$$\text{Rent} = \$60 \text{ plus } 30\% \times (280 - 225) = \$76.50$$

Flexing Rent on Price, Yield and Input Costs

Price and yield are both important. However, it is the margin over direct costs that pays rent.

Price volatility for input costs is increasing.

Including the cost of seed, fertilizer, pesticides and diesel, and drying fuel will further protect the margin for the operator.

Example

Base rent is multiplied by a factor for price, yield and input costs.

$$\text{\$60} \times (\text{current price} \div \text{base price}) \times (\text{current yield} \div \text{base yield}) \times (\text{base input costs} \div \text{current input costs}) = \text{current rent}$$

Example (Soybeans)

<u>Base</u>		<u>Current</u>
\$10.00	price	\$11.00
30 bu	yield	28 bu
\$94	input costs	\$100
\$60	rent	?

$$\$60 = (\$11.00 \div \$10) \times (28 \div 30) \times (\$94 \div \$100) = \$57.90$$