Flexible Farm Lease Agreements

Fluctuating markets and uncertain yields make it difficult to arrive at a fair cash rental rate in advance of each crop year. To address this problem, some owners and tenants use flexible lease agreements in which the rent is not determined until after the crop is harvested. The final rental rate is based on actual prices and/or yields attained each year. A recent survey showed that flexible leases accounted for nearly 12 percent of all cash leases in Iowa.

Flexible leases have the following advantages:

- The actual rent paid adjusts automatically as yields or prices fluctuate.
- Risks are shared between the owner and the tenant, as are profit opportunities.
- Owners are paid in cash – they do not have to be involved in decisions about crop inputs or grain marketing.

Option A: Share of Gross Revenue

The most common type of flexible lease calls for the owner to receive cash rent equal to a specified share of the gross revenue of the crop. The value of the crop is determined by multiplying the actual harvested yield by the market price available, usually at harvest time. Under this type of lease both price and yield risks are shared between tenant and owner, in the same proportion as the gross revenue. In this respect, it is similar to a crop share lease.

Most of the flexible leases in Iowa specify that the rent will be equal to anywhere from 25 to 40 percent of the gross crop value or gross crop revenue. Table 1 below shows average cash rents in Iowa as a percent of the gross crop value and revenue for the past 10 years. Gross crop value is the state average yield times the state average price from October through December. Gross crop revenue includes gross crop value plus all USDA commodity program payments and crop insurance indemnity payments. In recent years, these values have been nearly identical because only direct payments of about $20 to $25 per acre have been received from the USDA and crop insurance payments have been small.

Example 1 – Corn

- Cash rent will be equal to 25 percent of the gross crop revenue.
- The actual yield of corn is 150 bushels per acre, and the actual price is $6 per bushel.
- The gross income is equal to (150 x $6) = $900.
- The cash rent is equal to (25% x $900), or $225 per acre.

<table>
<thead>
<tr>
<th>Year</th>
<th>Iowa</th>
<th>Average Gross Crop Value</th>
<th>Cash Rent as % of Gross Crop Value</th>
<th>Average Gross Crop Revenue</th>
<th>Cash Rent as % of Gross Crop Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Corn</td>
<td>Soybeans</td>
<td>Corn</td>
<td>Soybeans</td>
</tr>
<tr>
<td>2004</td>
<td>$131</td>
<td>$371</td>
<td>$266</td>
<td>35%</td>
<td>49%</td>
</tr>
<tr>
<td>2005</td>
<td>$135</td>
<td>$311</td>
<td>$299</td>
<td>43%</td>
<td>45%</td>
</tr>
<tr>
<td>2006</td>
<td>$137</td>
<td>$460</td>
<td>$300</td>
<td>30%</td>
<td>46%</td>
</tr>
<tr>
<td>2007</td>
<td>$148</td>
<td>$595</td>
<td>$495</td>
<td>25%</td>
<td>30%</td>
</tr>
<tr>
<td>2008</td>
<td>$176</td>
<td>$744</td>
<td>$463</td>
<td>24%</td>
<td>36%</td>
</tr>
<tr>
<td>2009</td>
<td>$183</td>
<td>$672</td>
<td>$488</td>
<td>27%</td>
<td>36%</td>
</tr>
<tr>
<td>2010</td>
<td>$194</td>
<td>$766</td>
<td>$552</td>
<td>24%</td>
<td>33%</td>
</tr>
<tr>
<td>2011</td>
<td>$214</td>
<td>$984</td>
<td>$596</td>
<td>22%</td>
<td>36%</td>
</tr>
<tr>
<td>2012</td>
<td>$252</td>
<td>$952</td>
<td>$638</td>
<td>28%</td>
<td>40%</td>
</tr>
<tr>
<td>2013</td>
<td>$270</td>
<td>$731</td>
<td>$565</td>
<td>37%</td>
<td>48%</td>
</tr>
<tr>
<td>Average</td>
<td>$183</td>
<td>$657</td>
<td>$466</td>
<td>29%</td>
<td>40%</td>
</tr>
</tbody>
</table>

\(^1\) Cash Rental Rates for Iowa, AgDM File C2-10.
\(^2\) Iowa average yield x Iowa average cash price in Oct.-Dec.
\(^3\) Iowa average yield x Iowa average cash price in Oct.-Dec., plus USDA payments and crop insurance indemnity payments.

FM 1724 Revised May 2014
Option B. Base Rent plus Bonus

Another type of flexible lease formula specifies a base or minimum rent, plus the owner receives a share of the gross revenue in excess of a certain base value.

The base rent may be the amount that was being paid several years ago, before the recent increases in grain prices (see Table 1).

The base value for gross revenue can be the amount that would be received under typical yield and price conditions corresponding to the base rent (see Table 1). It can also be equal to the tenant’s cost of production per acre, including the base rent. This, in essence, becomes a profit-sharing plan.

The bonus may vary from one-third to one-half of the amount over the base revenue. Both parties must agree on how to calculate gross revenue and whether a gross revenue below the base level will cause the actual rent to be less than the base rent value. If the base rent is also specified as the minimum rent, it should probably be set lower than a typical fixed cash rent for the same land; otherwise, the landowner does not share in any of the downside risk.

Example 2 - Soybeans

- Base rent is $150 per acre.
- Tenant’s cost of production is $260 per acre, excluding land.
- Base gross revenue is $410 per acre ($150 + $260).
- Bonus is 35% of the gross revenue in excess of $410 per acre.
- Actual yield is 52 bushels of soybeans per acre and actual price is $13 per bushel.
- Gross revenue is equal to (52 bu. x $13) = $676 per acre.
- Revenue in excess of the base = $676 - $410 = $266.
- Rent is equal to $150 plus 35% of $266, or $150 + $93 = $243.
- However, if the market price of soybeans is only $9 per bushel, the gross revenue would be only $468, the bonus would be ($468 - $410) x 35% = $20, and the rent would be $170 per acre.

Sharing Risk

Owners and tenants should carefully consider the type and degree of risk they want to assume. Taking on risk means greater losses when prices or yields are low, but can result in larger profits in better years. Owners who wish to receive a fixed income from their farm investments may have to accept a lower long-term rent than those who are willing to share risk. Tenants with substantial financial obligations should consider adopting other means of reducing risk as well, such as purchasing crop revenue insurance.

Leases that base the rent on price only or yield only may actually increase the tenant’s risk in some years. This is because prices may be high when yields are low, or prices may be low when yields are high. Thus, adjusting the rent based on only one factor does not always reflect the actual profits received in that year. Adjusting the rent for changes in both price and yield ensures that the actual rent will be closely tied to the tenant’s income each year.

Determining Yield

It is important to agree ahead of time on the procedure for determining the factors that will be used to calculate the final rent. These factors should be based on information that is available to both parties. Actual yields can be determined by:

- weight tickets, if all the crop is sold or put into commercial storage
- combine yield monitors or weigh wagons
- storage bin capacity

When crops stored on the farm are ultimately sold, any variation from the estimated yield can be used to adjust the rent paid for that crop. Estimated yields should be corrected to a standard moisture level, for example, 15 percent moisture for corn.

Some flexible leases use the county average yield as estimated by USDA. This avoids the question of how to measure the actual production and removes the influence that above or below average management ability has on yields. However, county average yields are not generally announced until March each year.

Determining Price

The price used to calculate the final rent payment should represent the potential income that could be received from selling the crop. This can be the cash price at a local elevator or processor on a specified date, or an average of nearby prices on several dates. Prices on dates near or before the time the final rent is paid should be used even though the crop may actually be sold later. Only if the landowner is providing storage facilities should prices after harvest be used.

Forward contract prices available before harvest can be included, too. Many farm producers begin pricing
Flexible Farm Lease Agreements

to share indirectly in the benefits of this risk management tool. Of course, the landowner should share the cost, as well, meaning that crop insurance premiums should be deducted from the gross revenue used to calculate the rent, even in years when no indemnity payments are received.

Other Issues
Some tenants and landlords may want to avoid the possibility of a very high or very low rent in a given year by setting a maximum and/or minimum rent. This keeps the actual rent paid each year within a desirable range.

Many leases ask for a portion of the rent to be paid in advance, possibly by March 1. Under a flexible lease, the advance payment may be for a fixed amount while the final payment depends on actual prices and yields.

The flexible lease formula to be followed should be tested by using several different price and yield possibilities so as to illustrate the range of potential cash rents. Regardless of what type of agreement is adopted, it should be described in writing (with an example) and made a part of the written lease contract. The following page can be used as a lease supplement to specify flexible lease terms.

Other Resources
Iowa State University Extension and Outreach publication FM 1538/AgDM C2-12 contains a standard farm lease form. ISU Extension and Outreach publication FM 1801/AgDM C2-20 contains information on how to determine a fair cash rent.

An interactive spreadsheet to analyze flexible farm lease agreements is available on the Ag Decision Maker website at www.extension.iastate.edu/agdm/wholefarm/xls/c2-21flexiblerentanalysis.xlsx.

Government Payments
The Farm Service Agency (FSA) no longer specifies that, under a lease arrangement in which yield risk is shared between the tenant and the landowner, any USDA payments for which the farm may qualify must be shared in the same proportion as the risk. All payments are now paid to the tenant. In such cases, any such payments can be included in the gross revenue estimates used to determine the amount of rent due.

Crop Insurance Payments
Nearly 90 percent of Iowa’s corn and soybean acres are insured with multiple peril crop insurance. In years of low production and/or low prices, insurance indemnity payments can add significantly to a producer’s revenue. Including crop insurance payments in the gross revenue used to calculate the flexible rent allows the landowner

their crop in the spring or summer months. In that case, using the price offered for harvest delivery on one day per month from March through December, for example, may best reflect the overall value of the crop.

Another alternative to using a local price is to use a futures contract price minus a normal basis value for the location of the farm.

Other options include using the posted county prices calculated by FSA each day or the monthly average cash prices reported by the National Agricultural Statistics Service (NASS) Iowa branch.

<table>
<thead>
<tr>
<th>Example 3 - Determining Price</th>
</tr>
</thead>
<tbody>
<tr>
<td>Local elevator prices on:</td>
</tr>
<tr>
<td>April 1 (October delivery)</td>
</tr>
<tr>
<td>June 1 (October delivery)</td>
</tr>
<tr>
<td>October 1 (cash)</td>
</tr>
<tr>
<td>November 1 (cash)</td>
</tr>
<tr>
<td>December 1 (cash)</td>
</tr>
<tr>
<td>Average</td>
</tr>
</tbody>
</table>

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Prepared by
William Edwards, retired extension economist
Ann Johanns, extension program specialist

www.extension.iastate.edu/agdm
store.extension.iastate.edu
# Flexible Cash Rent Agreement

The amount of cash rent to be paid by the operator to the owner for the portion of the real estate designated as cropland shall be determined as follows (fill in the blanks where needed):

<table>
<thead>
<tr>
<th>Area of cropland</th>
<th>Corn</th>
<th>Soybeans</th>
<th>acres</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Option A</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Percent of gross revenue to share</td>
<td>___%</td>
<td>___%</td>
<td></td>
</tr>
<tr>
<td><strong>Option B</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Base rent per acre (if applicable)</td>
<td>$_______</td>
<td>$_______</td>
<td>per acre</td>
</tr>
<tr>
<td>Base gross revenue (if applicable)</td>
<td>$_______</td>
<td>$_______</td>
<td>per acre</td>
</tr>
<tr>
<td>Percent of gross revenue to share in excess of base</td>
<td>___%</td>
<td>___%</td>
<td></td>
</tr>
<tr>
<td>Minimum rent per acre (if applicable)</td>
<td>$_______</td>
<td>$_______</td>
<td>per acre</td>
</tr>
<tr>
<td>Maximum rent per acre (if applicable)</td>
<td>$_______</td>
<td>$_______</td>
<td>per acre</td>
</tr>
</tbody>
</table>

**Yield:** The actual yield used to calculate the rent shall be determined as follows: (check)
- ___ farm yield, determined by: ___ yield monitor ___ bin measurements ___ delivery receipt ___ other
- ___ county average yield as reported by NASS
- ___ other methods (describe):

**Price:** The actual price used to calculate the rent shall be determined as follows:

Source of price information to use ____________________________

Dates of prices to use ____________________________

**USDA Payments:** The value of any payments received as the result of participation in programs of the United States Department of Agriculture for the crop year for which the variable cash rent applies shall be divided as follows:

| a) | Owner ___% | Tenant ___% |
| b) | Owner ___% | Tenant ___% |
| c) | Owner ___% | Tenant ___% |

**Payment Dates:** The cash rent as determined by the above procedure shall be paid as follows:

<table>
<thead>
<tr>
<th>Date</th>
<th>Amount (fixed $ amount or flexible rent as calculated)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Examples or Actual Rent to Pay** (fill in numbers to show how the rent will be calculated)

<table>
<thead>
<tr>
<th><strong>Option A. Percent of gross income</strong></th>
<th><strong>Option B. Base rent plus bonus</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Yield</strong></td>
<td><strong>Corn</strong></td>
</tr>
<tr>
<td>x Price</td>
<td>$_______</td>
</tr>
<tr>
<td>= Gross crop value</td>
<td>$_______</td>
</tr>
<tr>
<td>+ Other payments</td>
<td>$_______</td>
</tr>
<tr>
<td>(USDA, insurance)</td>
<td></td>
</tr>
<tr>
<td>= Gross revenue</td>
<td>$_______</td>
</tr>
<tr>
<td>x % shared</td>
<td>___%</td>
</tr>
<tr>
<td>= Total rent per acre</td>
<td>$_______</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
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<td></td>
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<td></td>
<td></td>
</tr>
</tbody>
</table>
August 8, 2007

FLEXIBLE CASH LEASES BASED ON CROP INSURANCE PARAMETERS

Commodity prices likely will be more variable over the next several years than in previous years. Variable commodity prices cause difficulties in setting cash rents as farmland returns will vary because of commodity price changes. Flexible cash rent leases may aid in setting rents in a variable commodity price environment.

In this article, a flexible cash lease is proposed that bases its payments on parameters used in setting revenue guarantees on Group Risk Income Plan (GRIP) crop insurance policies. As structured, this flexible lease causes landlords and farmers to share in commodity price changes that occur between years. Generally, hedging is not effective at reducing risks associated with between year price changes. As structured, the lease causes farmers to bear all risks associated with yield shortfalls and price changes within the year. If desired, farmers can use crop insurance and hedging to offset some of the risks associated with yield shortfalls and price changes within the year.

The simplest form of the payment mechanism for this lease is first described. Advantages and disadvantages then are discussed. Finally, modifications to the payment mechanism are described.

**Example of Setting Cash Rent Payments**

In its simplest form, the payment mechanism based on corn is:

\[
\text{Expected county corn yield} \times \text{base corn price} \times \text{rent factor.}
\]

The variables in this formula are:

1. The **expected county yield** is set by the Risk Management Agency (RMA) for each crop in each county. This parameter represents an estimate of the most likely county corn yield. In most years, RMA revises expected yields based on histories of county yields.

2. The **base price** is released by RMA at the beginning of March. The base price equals the average of the February settlement prices on the December corn contract traded on the Chicago Board of Trade (CBOT). The base price is used in setting revenue guarantees on GRIP, Crop Revenue Coverage (CRC) and Revenue Assurance (RA).

3. The **rent factor** is a percentage negotiated between the landlord and farmer. It represents the share of county revenue received by the landlord.

As an example, take a farm in Macon County in 2007. In 2007, the expected county corn yield in Macon County is 178.8 bushels and the base price is $4.06 per bushel. If the landlord and farmer negotiate a .35 rent factor, the cash rent is $254 per acre (178.8 bushel county yield x $4.06 base price x .35 rent factor).
A history of cash rents for Macon County is shown in Table 1 for rent factors of .3, .35, and .4. For a rent factor of .35, cash rents vary from a low of $133 in 2001 up to a high of $254 in 2007. Cash rents would have averaged $158 per acre for a .35 rent factor.

### Table 1. Flexible Cash Rent Example for Macon County, Illinois.

<table>
<thead>
<tr>
<th>Year</th>
<th>Expected Yield</th>
<th>Base Price</th>
<th>Expected County Revenue</th>
<th>Rents for Different Factors ¹</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>0.3</td>
</tr>
<tr>
<td>1999</td>
<td>162.5</td>
<td>$2.44</td>
<td>$397</td>
<td>$119</td>
</tr>
<tr>
<td>2000</td>
<td>164.3</td>
<td>2.54</td>
<td>417</td>
<td>125</td>
</tr>
<tr>
<td>2001</td>
<td>165.3</td>
<td>2.30</td>
<td>380</td>
<td>114</td>
</tr>
<tr>
<td>2002</td>
<td>168.8</td>
<td>2.30</td>
<td>388</td>
<td>116</td>
</tr>
<tr>
<td>2003</td>
<td>168.8</td>
<td>2.38</td>
<td>402</td>
<td>121</td>
</tr>
<tr>
<td>2004</td>
<td>167.0</td>
<td>2.93</td>
<td>489</td>
<td>147</td>
</tr>
<tr>
<td>2005</td>
<td>170.4</td>
<td>2.38</td>
<td>406</td>
<td>122</td>
</tr>
<tr>
<td>2006</td>
<td>179.4</td>
<td>2.59</td>
<td>465</td>
<td>139</td>
</tr>
<tr>
<td>2007</td>
<td>178.8</td>
<td>4.06</td>
<td>726</td>
<td>218</td>
</tr>
<tr>
<td>1999-2006 average</td>
<td>$418</td>
<td></td>
<td></td>
<td>$125</td>
</tr>
<tr>
<td>1999-2007 average</td>
<td>$452</td>
<td></td>
<td></td>
<td>$136</td>
</tr>
</tbody>
</table>

¹ Rent equals expected yield x base price x rent factor.

### Advantages of Flexible Cash Rents Based on Crop Insurance Parameters

1. Cash rents will vary as prices change between years. Higher base prices will result in higher cash rents and vice versa.

2. Cash rents are determined when crop insurance decisions are made. Farmers can use crop insurance and hedging to protect against yield shortfalls and within year price declines.

3. Information needed to determine cash rents is available from the RMA website (www.rma.usda.gov) in either the actuarial document section or from the RMA premium calculator. In addition, expected county yields and base prices are available from the *Premium Calculator* in the crop insurance section of *farmsdoc*. Because information is readily available, chances of disputes between landlords and farmers over variables are minimized.

4. The lease does not require any data from the farm being leased. Nor does the lease require keeping track of prices. Hence, administrative costs associated with determining cash rents are low.

5. The level of the cash rent will be known relatively early in the production year.

6. The Farm Service Agency will regard this lease as a cash lease. Hence, direct and counter-cyclical payments do not have to be shared between the landlord and tenant.
Disadvantages of Flexible Cash Rents Based on Crop Insurance Parameters

1. Under this lease, farmers still bear considerable yield and price risk. The lease only adjusts for risks associated with between year price changes. Farmers face all the risk of within year price changes and yield shortfalls. Similar to all flexible cash leases, this lease is not as good at sharing returns as is a crop share lease.

2. Over time, the rent factor may have to be adjusted to account for changes in costs and risks. This lease only adjusts rent payments based on price changes and expected yield changes. Also impacting returns are costs. As costs increase, the rent factor would need to be adjusted down. In addition, risk levels should impact the rent factor. As risk increases, the rent factor should be adjusted down.

3. The actual cash rent will not be known until the spring in the year of production. Many cash rents are negotiated prior to this point. Hence, rent determination may be later than from other leases.

Determining the Rent Factor

Rent factors will need to be negotiated between the landlord and tenant. In general, farms with lower productivity relative to the county average should have lower rent factors and vice versa.

Modifications to the Lease

Several modifications could be included in the leasing arrangement:

1. The minimum cash rent can be specified. For example, a lease could have a minimum cash rent of $140 per acre. If the formula gives a cash rent below $140 per acre, the cash rent would be $140.

2. The maximum cash rent can be specified. The maximum cash rent could be set at $250 per acre. If the formula results in a cash rent above $250, the cash rent would be $250.

3. All crops grown on the farm can be used in calculating the gross revenue. The above formula bases rent only on corn. Soybean and wheat revenue could also be used in calculating the rent. The rent could be based on the proportion of crops typically grown on the farm. The following formula shows an example for corn and soybeans grown in a 50-50 rotation:

\[(\text{Expected county corn yield} \times \text{base corn price} \times 0.5) + (\text{expected county soybean yield} \times \text{base soybean price} \times 0.5) \times \text{rent factor}.\]

Table 2 shows an example of rent payments for Macon County based on both corn and soybean revenue.

4. Rent payments can be based on harvest prices and actual county yields which are used to calculate revenue for GRIP. Harvest prices are based on settlement prices of CBOT contracts in the fall. Using harvest prices and actual yields will shift some of the within year price and yield risk to the landlord. Several caveats relative to using harvest prices and actual county yields are:

   a. Actual county yields are not released until February or March in the year following production. Hence, the lease payment will not be known until the year following production. For example, the cash rent for the 2007 cropping year will not be known until February or March in 2008.

   b. RMA releases two harvest prices. One is used for GRIP and Crop Revenue Coverage (CRC) while the other is used for Revenue Assurance (RA). The lease contract needs to specify which harvest price should be used in determining cash rents.
c. For crops in Illinois, RMA uses a different county yields in calculating GRIP payments than is commonly reported by the National Agricultural Statistical Service (NASS). RMA uses a county yield equal to total crop production in the county divided by planted acres. NASS typically reports crop production in a county divided by harvested acres. The lease contract needs to specify which county yield should be used in determining cash rents.

Table 2. Flexible Cash Rents for Macon County Based on Corn and Soybean Expected Revenue.¹

<table>
<thead>
<tr>
<th>Year</th>
<th>Corn Expected Yield</th>
<th>Corn Base Price</th>
<th>Corn County Revenue</th>
<th>Soybeans Expected Yield</th>
<th>Soybeans Base Price</th>
<th>Soybeans County Revenue</th>
<th>Rents for Different Factors¹</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td>0.3</td>
</tr>
<tr>
<td>1999</td>
<td>162.5</td>
<td>$2.44</td>
<td>$397</td>
<td>47.1</td>
<td>$4.95</td>
<td>$233</td>
<td>$94</td>
</tr>
<tr>
<td>2000</td>
<td>164.3</td>
<td>2.54</td>
<td>417</td>
<td>47.5</td>
<td>5.36</td>
<td>255</td>
<td>101</td>
</tr>
<tr>
<td>2001</td>
<td>165.3</td>
<td>2.30</td>
<td>380</td>
<td>48.0</td>
<td>4.59</td>
<td>220</td>
<td>90</td>
</tr>
<tr>
<td>2002</td>
<td>168.8</td>
<td>2.30</td>
<td>388</td>
<td>48.5</td>
<td>4.53</td>
<td>220</td>
<td>91</td>
</tr>
<tr>
<td>2003</td>
<td>168.8</td>
<td>2.38</td>
<td>402</td>
<td>48.9</td>
<td>5.23</td>
<td>256</td>
<td>99</td>
</tr>
<tr>
<td>2004</td>
<td>167.0</td>
<td>2.93</td>
<td>489</td>
<td>49.0</td>
<td>7.27</td>
<td>356</td>
<td>127</td>
</tr>
<tr>
<td>2005</td>
<td>170.4</td>
<td>2.38</td>
<td>406</td>
<td>49.2</td>
<td>5.99</td>
<td>295</td>
<td>105</td>
</tr>
<tr>
<td>2006</td>
<td>179.4</td>
<td>2.59</td>
<td>465</td>
<td>51.5</td>
<td>6.18</td>
<td>318</td>
<td>117</td>
</tr>
<tr>
<td>2007</td>
<td>176.8</td>
<td>4.06</td>
<td>726</td>
<td>49.8</td>
<td>8.09</td>
<td>403</td>
<td>169</td>
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<tr>
<td></td>
<td>1999-2006 average</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td></td>
<td>1999-2007 average</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>$110</td>
</tr>
</tbody>
</table>

¹ Rents equal (expected corn county revenue x .5 + expected soybeans county revenue x .5) x rent factor.

Examples for Other Illinois Counties

A Microsoft Excel spreadsheet that calculates yearly cash rents for different rent factors is available from the farmdoc website: click here to download.

Tables similar to those presented above are available all counties in Illinois with GRIP insurance.

Summary

Flexible cash leases based on GRIP parameters shifts some of the risks associated with between year price changes to the landlord. Risks associated with within year price changes and yield shortfalls are born by the farmer. This lease is appropriate for cases in which only the transfer of between year price changes are desired. If risk shifting associated with within year price changes and yield shortfalls is desired, cash rents based on a farm’s revenue likely would be more appropriate.

Issued by: Gary Schnitkey and Dale Lattz, Department of Agricultural and Consumer Economics
ILLINOIS FARM LEASES: ONE VARIABLE CASH RENT OPTION
By Donald L. Uchtmann and A. Bryan Endres*

Abstract: This article describes a Variable Cash Rent Lease in which the farmland owner and operator negotiate a Base Cash Rent based on expected corn yields and the current price for new-crop corn futures contracts. The Actual Cash Rent will be the Base Cash Rent adjusted for changes in corn futures prices between the time the lease is negotiated and about March 1. The principal advantage of such a lease is that it allows a landowner and farm operator to negotiate a lease much earlier in the fall because the rent automatically adjusts for changes in futures prices occurring after lease negotiation but before Spring planting. The article also provides one example of key language for calculating the variable cash rent under the lease. However, the parties should seek legal counsel before using such a lease or the sample language. This article is part of a law-related educational program for Illinois family farmers made possible by a gift from the Illinois Bar Foundation. The assistance of the Agricultural Law Section Council of the Illinois State Bar Association in reviewing the article also is appreciated.

Introduction
Fluctuating commodity prices, such as those witnessed in 2007-2008, create difficulties for landowners and operators in setting fair cash rents because gross revenues from the rented farm will vary significantly depending on what happens to commodity prices. Farm tenants and owners, however, can tailor the traditional cash lease to “automatically adjust” to changing price scenarios. A “variable cash rent” lease is one way in which both the farm operator and farm owner can share in the benefits of unanticipated increases in commodity prices, as well as the adverse financial impact of falling prices.

A 2007 farmdoc article by Schnitkey and Lattz titled Flexible Cash Leases Based on Crop Insurance Parameters describes several specific variable cash rent arrangements. Click here [http://www.farmdoc.uiuc.edu/manage/newsletters/fe007_13/fe0007_13.pdf] to see this farmdoc article. Schnitkey and Lattz propose that landowners and operators consider a lease in which the amount of the cash rent is determined by parameters used in setting revenue guarantees on Group Risk Income Plan (GRIP) crop insurance policies, i.e., the amount of rent is based on county yields and prices for futures contracts traded on the Chicago Board of Trade.

The purpose of this Agricultural Law and Taxation Brief is to further discuss the Flexible Cash Rent concept proposed by Schnitkey & Lattz and to provide one example of language that could be used to modify a traditional Cash Lease between a landowner and farm operator. Because there are numerous factors to consider, landowners and farm operators should seek legal counsel before deciding to use such a lease.

The Core Idea of the Variable Cash Rent Lease Described in this Article
The basic idea of the Variable Cash Rent Lease described below is that ...
- A Base Cash Rent/Acre is negotiated based on expected yields, current prices, and other factors specific to the farm.
- The Base Cash Rent is adjusted later by an indexing factor reflecting changes in Futures Prices occurring between the time the Base Cash Rent is negotiated and about March 1 when the Actual Cash Rent is “set”.
- Changes in Futures Prices will be determined from readily available Crop Insurance data published by USDA’s Risk Management Agency (www.rma.usda.gov).

There are many potential measures of price and yield that could be used in variable cash rent lease arrangements. For example, changes in new-crop futures prices could be based on one crop, e.g., corn, or on multiple crops, e.g., corn and soybeans, and the futures prices could be based on several potential time periods, e.g., the
period ending just before March 1 and/or the period ending just after harvest. The cash rent also could be adjusted for actual yields (county average or specific farm) that are higher or lower than expected and for unanticipated changes in input costs. However, in this article, the authors have chosen to illustrate the variable lease concept by “flexing” only for changes in the futures price for corn occurring after the lease is signed but before March 1. In effect, the authors have chosen to illustrate the concept of the variable cash rent lease with a relatively simple conceptual approach.

Example – Cash Rent Adjusts Only for Changes in the Futures Price of Corn

The Lease. On October 1, 2008, Landowner and Farm Operator negotiate a lease for a 100 acre farm for the 2009 crop year. They agree to a “Base Cash Rent” of $20,000 ($200 per acre) based on their expectations of yields and prices for the new crop, and other factors such as the productivity of the farm, its proximity to cash markets, anticipated input costs for the operator, and the local “rental market” for farmland.

The “Actual Cash Rent” paid by the operator will be the “Base Cash Rent” adjusted for any change, up or down, in the price of the December 2009 corn futures contract on the Chicago Board of Trade. The change in price will be the difference between the futures contract price on the day nearest the date of lease signing (the futures price can be obtained at www.farmdoc.uiuc.edu) and the average trading price of the same futures contract (the December 2009 corn contract) during February.1

Determining the Actual Cash Rent. Assume that on October 1, 2008 (the day the variable cash rent lease was signed), the “settlement price” for the December 2009 corn futures contract on the CBOT is $6.50/bushel (futures prices are available from the farmdoc Website). Also assume that in early March of 2009 USDA’s Risk Management Agency publishes the “Expected Price”, also known as the “base price”, for corn and this price is $7.15/bushel (this price is used in calculating “GRIP” Crop Insurance, is published on the RMA Website, and will be the average trading price during February 2009 of the December 2009 corn futures contract). The “Actual Cash Rent” per acre is now “set” at 1.10 x $200/acre, where 1.10 = $7.15/$6.50. The Actual Cash Rent is 10% higher than the Base Cash Rent because the futures price for new crop corn rose 10% between the time the lease was negotiated and the time RMA calculated the “Expected Price”, also known as “Base Price”, in early March.

Comparison to a “Crop Share” Lease. With the Variable Cash Rent Lease described above, the income of Landowner fluctuates in much the same manner as the income of a landowner with a share lease, assuming yields are normal and input costs are “locked in” at the lease signing.

Advantages of This Variable Cash Rent Lease

The principal advantage of the variable cash lease described above is that it allows a landowner and farm operator to negotiate a fair lease much earlier in the fall preceding the crop year because the rent automatically adjusts for changes in futures prices occurring after the lease is negotiated, but before Spring planting.

For example, assume that in October 2008 our Tenant in the previous example was anxious to renew the cash lease at a reasonable rent because Tenant wanted to pre-purchase seed, fertilizer, etc. and to start fall tillage. Owner was reluctant to sign a lease at this time because a fair cash rent based on historic yields and the October outlook for “new crop” prices might not be a fair lease a few months later if “new crop” futures prices rise. Owner and Operator resolved this timing problem by deciding to use a variable cash rent lease instead of a traditional fixed cash lease. Both realized that if they signed a
variable cash lease that was fair based on the October outlook for prices, and would “flex” the rent upward if new crop prices rose and downward if prices fell, there was no need to delay signing the lease.

Other advantages of this particular variable cash rent lease are:

- The information needed to “set” the rent is readily available on the Internet, thanks to USDA’s Risk Management Agency and farmdoc.
- All the needed data for this lease will be available about March 1 – at the start of the crop year – because this lease only adjusts for futures price changes occurring between the time the parties sign the lease and the end of February.
- Although the yield risk is borne by the farm operator, the rent is “set” at about the same time that the operator is managing risk by making crop insurance decisions.
- The variable cash rent lease is likely to be signed earlier than a fixed cash rent lease; this will give operator more time to lock in prices and otherwise manage input costs.

Some Factors to Consider before Deciding to Use a Variable Cash Rent Lease

The exact nature of a farm lease can have legal implications far beyond the profit or loss of the farm operator and the net amount of rent received by the farmland owner. Some of the implications of a variable cash rent lease are described below.

Estate Planning and SE Tax Implications. Whether the lease is structured to preserve eligibility for “Agricultural Use Valuation” in a deceased landowner’s estate may be important. Also, whether the lease is structured to cause the rent received to be “Self Employment Income” can have significant tax management implications. These are just two examples of the many considerations that may be important to a farmland owner and should be discussed with a legal advisor.

Risk Sharing Implications. Farming is a risky business and the nature of the lease determines how yield and price risks are shared (or not shared) between the owner and tenant.

In the typical “Crop Share” lease, both parties share the risks of low yields or crop prices because the landowner’s rent is a predetermined share of the crop actually produced. When yields or prices are good, both the landowner and operator benefit. When yields or prices are bad, both suffer. In contrast, with the typical fixed “Cash” lease, the landowner receives the agreed upon cash rent regardless of whether yield and crop prices are high or low. Thus the tenant bears all the risks associated with price and yield variability (and input cost variability).

Farm operators and owners are exploring ways in which the cash lease can “automatically adjust” to changing price scenarios. However, making the cash rent payments dependant on changing price or yield scenarios also can affect whether the tenant and farmland owner must divide farm program payments.

Farm Program Payment Implications. Whether a farm lease meets the technical definition of a “cash” or a “share” lease under applicable federal regulations determines whether the farm operator, alone, or both the operator and the farmland owner receive certain USDA farm program payments. “Flexible” or “adjustable” cash rental arrangements can be especially problematic. ALTB 06-01, available on the farmdoc Website, discusses this important implication. (Click Here for ALTB-06-01 [http://www.farmdoc.uiuc.edu/legal/articles/ALTBs/ALTB_06-01/ALTB_06-01.pdf]).

The Schnitkey and Lattz proposal for a variable cash rent based on federal crop insurance parameters (e.g., the rent is based on expected or actual county yields and/or futures prices determined on the Chicago Board of Trade) appears to be a “cash lease” under federal regulations because the amount of rent is not dependent on actual yields on the rented farm or actual prices received for the crops grown.
However, this matter and other legal issues should be discussed with your attorney.

As a practical matter, there are many different variable cash rent possibilities and many local Farm Service Agency offices reviewing farm leases. Thus, the initial determination by the FSA about whether a particular lease is a "cash lease" or a "share lease" can not be predicted with complete certainty.

It is possible that the administrative rules might change for the 2009 or later crop years. If, for example, new rules allowed the landlord and tenant to agree about how the farm program payments were to be divided, the classification of the lease as a "share" lease or a "cash" lease would be less significant.

Resolving Key Questions

If, after considering all implications, an owner and operator decide to consider a variable cash rent lease like the one described in this article, they must resolve key questions. A checklist follows.

1. What commodity will be used to determine changes in commodity prices? (A simple approach would be to focus only on corn and changes in the price of the "new-crop" December futures contract between the time the Base Cash Rent is negotiated and about March 1. The "Expected Price" for corn, also known as the "Base Price", used in GRIP Crop Insurance is released by RMA in early March, based on the February trading of "new crop" futures contracts. This is the approach of this article.)

2. Is any rent to be paid "up front" and, if so, how much and when? (March 1 is one date to consider for an "up front" rent payment.)

3. When is the balance of the cash rent to be paid? (September 1 or December 1 or another of many possibilities.)

4. Is there a "floor" on the variable cash rent? (A floor might be desired by the landowner. Any "floor" generally should be not less than any "up-front" rent payment.)

5. Is there a "cap" on the variable cash rent? (A cap might be desired by an operator wishing to limit operator's risk if widespread drought results in much lower than expected yields and high prices. Some would argue that if there is a floor on the variable rent, their also should be a cap.)

Possible Language for the Lease

The key language in a Variable Cash Lease is the description of how to calculate the variable cash rent. Otherwise, the Variable Cash Lease is similar to the traditional "fixed" Cash Lease. One possibility is for the "amount of cash rent to be paid" clause to refer to an appendix that further describes in detail the calculation of the variable cash rent. Alternatively, the "amount of cash rent to be paid" clause in the lease could describe how to calculate the rent. In Appendix A to this article the authors include possible language describing variable cash rent calculations. You should discuss this potential language with your legal advisor.

The Importance of Communication about How the Dollar Amount of the Actual Cash Rent Has Been Determined

Memories may fade. Therefore, a farm operator with a variable cash rent lease should help the farmland owner understand the final calculations for determining Landowner's rent check. A letter accompanying the final rent payment provides one opportunity to explain why the payment is what it is. A sample letter, based on our earlier example, i.e., based on the Base Cash Rent of $20,000 and a hypothetical futures price scenario previously noted, is provided below. The sample letter can be adapted as appropriate for your particular lease. Reading the sample letter now may provide you with additional insights into how the variable cash rent lease described above might actually work in practice.
******

Dear Farmland Owner:

I am happy to enclose a $7000 check as the final cash rent payment for your farm. This amount represents:

- the $20,000 "Base Cash Rent" we agreed to last October,
- multiplied by a 1.10 Variable Cash Rent Indexing Factor (explained below),
- less the $15,000 advance rent payment that I made on March 1, 2009.

Please recall that the variable cash rent lease we signed last October stated that the "Base Cash Rent" for the farm was $20,000 and that the Actual Cash Rent would be the "Base Cash Rent" multiplied by the "Variable Cash Rent Indexing Factor". We decided on a Base Cash Rent of $20,000 because of various factors, including our expectations of new crop corn prices. We also knew that prices could move up or down between October 1, 2008 (when we signed the lease) and March 1, 2009 (when my current lease term for your farm began) so we decided to adjust the "Base Cash Rent" upward or downward depending on what happened to the futures price of corn during that time period. We also agreed that I would make a $15,000 rent payment on March 1.

Under our lease, the "Variable Cash Rent Indexing Factor" is A/B, where B was the assumed base price for corn when we signed the lease. Please recall that we checked the Farmdoc website (www.farmdoc.uiuc.edu) on the evening we signed the lease to see the "Settlement Price" for the December 2009 Corn Futures Contract at that time. That settlement price was $6.50 and we recorded $6.50 in our lease as our Assumed Base Price for corn. Therefore, "B" (Our Assumed Base Price for Corn) in the formula "A/B" is $6.50.

We also agreed that "A" would be the "Actual Base Price" (also known as the "Expected Price") for Corn for GRIP crop insurance purposes. In early March, USDA's Risk Management Agency calculated this price which was based on the average price of the December 2009 Corn Futures Contract during the month of February 2009. This price, $7.15, was published on the Risk Management Agency's Website in early March. You can verify this price ($7.15 - "A" in our formula) by visiting the RMA website. The specific Internet address is [insert correct Web address for 2009 price - FYI, the 2008 price was available at http://www.rma.usda.gov/bulletins/rd/2008/08-012.pdf].

With this background, it is now apparent why the enclosed check is for $7000:

- We agreed that $20,000 would be our Base Cash Rent for 2009.
- We also agreed that Actual Cash Rent would be the Base Rent of $20,000 multiplied by our "Variable Cash Rent Indexing Factor", A/B
- As described in preceding paragraphs, A is $7.15 and B is $6.50, so the "Variable Cash Rent Indexing Factor" = $7.15/$6.50 = 1.10
- Actual Cash Rent = $22,000 ($20,000 x 1.10)
- Since I made a $15,000 rent payment on March 1, the balance that I owe is $7,000 (i.e., $22,000 minus $15,000 already paid).

One advantage of this variable cash rent approach is that we could sign our lease much earlier than if we had waited until March 1 because of uncertainty about how much grain prices might rise or fall between October and March. I think being able to sign the lease earlier rather than later because the rent automatically "flexes" for changes in price is good for both of us. From my standpoint, for example, I was better positioned to do necessary field work in the fall, and to order in a timely manner the seed and fertilizer used on your farm - all because we signed the lease in October rather than March.

I look forward to working with you in the coming year.

Yours truly,
Farm Operator
******
Summary

This article describes a Variable Cash Rent Lease in which a Base Cash Rent is negotiated based on expected corn yields and the current price for the new-crop corn futures contract. The Actual Cash Rent will be the Base Cash Rent adjusted for changes in corn futures prices between the time the lease is negotiated (this price is available from the farmdoc Website – www.farmdoc.uiuc.edu, for example – and should be stated in the lease when signed) and about March 1 (this price is reported on USDA’s Risk Management Agency (RMA) Website).

Appendix A contains possible language for the lease – language explaining how to determine this Actual Cash Rent. The preceding section of the article also contained a sample end-of-year letter from Operator explaining how the Actual Cash Rent in our example was calculated.

The principal advantage of this variable cash rent lease is that it allows a landowner and farm operator to negotiate the lease much earlier in the fall because the rent automatically adjusts for changes in futures prices. Another advantage is that the needed price data is readily available via the Internet.

Although the operator and owner share price risk in this variable cash rent lease, the operator continues to bear all the yield risk and the risk of higher than anticipated input costs like fuel and fertilizer. If the parties had used a crop share lease, rather than this variable cash rent lease, all three risks – price variability, yield variability, and input cost variability – would have been shared by both operator and owner.

Many other approaches to a variable cash rent lease are possible. For example, the rent also could be adjusted for changes in the county yield (this data probably would not be available from USDA’s Risk Management Agency until well into the new calendar year following harvest) or actual farm yields (but this may adversely affect how farm program payments are paid).

The adjustment in rent also could take into account changes in commodity prices occurring during the growing season (although under this approach, the rent probably could not be “set” until about December 1 of the crop year). The rent also could flex based on changes in prices or yields of more than one commodity.

In this article, the authors have chosen to illustrate the variable cash rent concept with a relatively simple approach – rent is adjusted for changes in the futures price of corn, only, occurring between the time the lease is signed and the about March 1.

In the authors’ opinion, all leases for Illinois farmland should be in writing as a general rule, but having a written lease is even more important when the lease is a variable cash rent lease. Just imagine the difficulty of explaining why the final rent payment is a certain amount without being able to refer back to the written lease and its description of how the Actual Cash Rent is to be determined.

Legal counsel can be very helpful in identifying important issues, negotiating the lease, and adapting the terms to the client’s needs. It is generally a good idea to seek legal counsel in negotiating a lease for farmland. It is even more important to do so, in the authors’ opinion, when the lease is a variable cash rent lease.

*Urchmann is a Professor Emeritus and Endres is an Assistant Professor in the Agricultural Law Group of the Department of Agricultural and Consumer Economics, University of Illinois at Urbana-Champaign. The authors thank Prof. Gary Schnitkey for his assistance in preparing the article and attorneys Michael A. Mattingly and Q. Anthony Siemer, members of the ISBA Agricultural Law Section Council, for their helpful review. AGRICULTURAL LAW AND TAXATION BRIEFS are available at www.farmdoc.uiuc.edu/legal/.
Appendix A – Describing How the Variable Cash Rent Is Determined
(This or similar language could be inserted directly into the lease or included as an appendix to the lease – see back of Appendix A for instructions/comments – legal counsel is recommended – actual numbers appearing in the blanks below correspond to the Example previously described)

AMOUNT OF ACTUAL CASH RENT AND MANNER OF PAYMENT

Amount of Actual Cash Rent

ACTUAL CASH RENT is:
The BASE CASH RENT multiplied by the VARIABLE CASH RENT INDEXING FACTOR, each as described below, subject to the minimum and maximum limitations also described below.

BASE CASH RENT: The Base Cash Rent is $20,000 ($200/acre x 100 acres)

The Base Cash Rent assumes that the Base Price* for corn, also known as the “Expected Price”**, in the crop year(s) covered by this lease, is $6.50 per bushel.

*The actual Base Price will be determined by USDA’s Risk Management Agency for purposes of GRIP crop insurance (USDA calculates and publishes Base Price, also known as “Expected Price”, in early March based on the average trading price on the Chicago Board of Trade of the December Corn Futures Contract during the month of February). The best predictor of the Base Price for corn will be the most recent trades on the Chicago Board of Trade of this futures contract.

VARIABLE CASH RENT INDEXING FACTOR: Variable Cash Rent Indexing Factor = A/B, where ...
A = Actual Base Price (a/k/a “Expected Price”) for Corn for GRIP crop insurance, and
B = Assumed Base Price for Corn (i.e., the price inserted into the blank above)

[For example, if A = $7.10 and B = $6.50, then the indexing factor, A/B, is $7.10/$6.50 = 1.10. Note that the Indexing Factor could be greater or less than 1.00, depending on whether corn futures prices rise or fall after the lease is negotiated.]

MINIMUM AND MAXIMUM LIMITATIONS (insert if applicable): Actual Cash Rent shall be ...
not less than $15,000 ( $150/acre x 100 acres), and
not more than $30,000 ( $300/acre x 100 acres).

Timing of Rent Payments and Manner of Payment

The first $15,000 of the Actual Cash Rent will be paid on or before March 1, 2009. The balance, if any, shall be paid on or before December 1, 2009 of the lease year.

[*† Assumed to have been agreed to in the Example, even though not expressly stated.]
Instructions/comments regarding the Variable Cash Rent Lease Form
(this particular lease flexes for changes in the price of corn, only)

1. Landowners and farm operators should seek legal counsel concerning a farm lease, as a
general rule. Legal counsel is even more important for a variable cash rent lease.

2. The key language in a Variable Cash Lease is the description of how to calculate the variable cash
rent. Otherwise, the Variable Cash Lease is similar to the traditional “fixed” Cash Lease. Potential
language for the other sections of the Variable Cash Lease can be found at
http://www.farmdoc.uiuc.edu/legal/articles/MSWord/CashLeaseDLU01-0911.doc

3. Determining Base Cash Rent: Operator and Owner should agree on a base cash rent for the farm,
based on their expectations of yields and prices for the new crop and other important factors such as
the productivity of the farm, its proximity to cash markets, input costs expected by the operator,
property taxes to be paid by the owner, and the local “rental market” for leased farmland. Insert into
the form the total Base Cash Rent, the Base Cash Rent per acre, and the number of acres covered by
the Base Cash Rent.

4. Documenting the assumed Base Price of Corn (New-Crop December Futures Price) when the Lease is
Negotiated: The base cash rent will be adjusted upward or downward by a “variable cash rent index”
determined by changes in the futures price for “new crop” occurring after the lease is negotiated
but before planting. Operator and Owner should record the assumed “Base Price” for corn by
inserting the price per bushel for the most recent trades on the Chicago Board of Trade of New-Crop
December Futures Contracts for corn. [Go to farmdoc home page (http://www.farmdoc.uiuc.edu/),
click on “Futures and Options Contracts”, and select futures contracts for corn. Choose the December
contract for the applicable crop year and select the settlement price on or nearest the day the lease is
signed. Record the number in the lease. It will be needed later when Actual Cash Rent is calculated.]

5. Minimum and Maximum Limitations: If the owner and operator wish to set a floor and/or a
ceiling on the amount of rent to be paid, regardless of adjustments the variable cash rent
index might otherwise require, insert such minimum and maximum limitations. If no such
limitations are desired, insert N/A (Non Applicable) into the blanks.

6. Document the Timing Manner of Rent Payments: Complete as appropriate. Normally, any
“up-front” rent payment would not exceed any “minimum” payment limitation.

7. Determining the Variable Cash Rent Index and the Annual Cash Rent: The Annual Cash
Rent is the Base Cash Rent multiplied by the Variable Cash Rent Index. The index is the
“Actual Base Price for Corn for purposes of GRIP crop insurance” divided by the “Assumed
Base Price for Corn used in determining the Base Cash Rent”. If, for example, the Actual
Base Price, also know as the “Expected price”, for Corn (calculated by USDA’s Risk
Management Agency for GRIP Crop Insurance; based on the February trading of the new-
crop December Futures Contracts for corn; available in early March) was 110% of the
assumed base price used in determining Base Cash Rent, the Annual Cash Rent would be
1.10 x Base Cash Rent. [The Base Price for corn, also known as the Expected Price for corn,
is published on the Risk Management Agency Home Page (http://www.rma.usda.gov/) in
early March.]
Flexible cash farm leases

A decline in crop prices compared to recent years is expected this fall. Despite lower prices, many tenant operators could pay higher fixed cash rental rates in 2014 and beyond. Most landowners recognize the need to create a reasonable cash rental rate as tenant operators assume most production and crop risks.

Since 2010, Iowa cash rental rates have increased by nearly 47 percent. The statewide average cash rent in 2013 is estimated at $270 per acre, with even higher amounts for more productive farmland. However, much of the increase in cash rental rates was fueled by cash crop prices that averaged $5 to $7 per bushel for corn and $11 to $14 per bushel for soybeans over the past three years. The USDA midpoint cash price for the 2013 crop is currently forecast at $4.80 per bushel for corn and $10.75 per bushel for soybeans.

A 2010 survey of Iowa farmland owners indicated that 16 percent of cash rented farms use a flexible arrangement. Landowners who adopt a flexible cash farm lease typically receive a guaranteed base cash rent amount, in addition to a potential flex payment triggered by higher gross revenue (yield times price). The use of a flexible cash farm lease is likely fairer to both the landowner and tenant. However, the challenge is coming up with a base rent amount, maximum cash rent, and a way to determine a flexible payment that both parties understand and deem fair.

Determining yield and prices

Establishing a farm’s actual yield (dry weight for corn adjusted to 15 percent) might require that lease arrangements reflect grain bin measurements, scale tickets, settlement sheets, yield monitor data, grain car scales, or other verifiable methods. To simplify, the yield information required should be the same as the Actual Production History (APH) provided annually for crop insurance purposes. A copy of a farm’s actual proven yield for APH purposes should be provided to the landlord by Dec. 1 to calculate the farm’s flexible cash rent.

Averaging a series of harvest delivery bids at a local co-op or elevator is worth consideration for establishing the crop price on a flex lease. Such a price overcomes the potential low harvest price bias, and can be designated for select months during the year. This is a price that tenants could receive should they decide to forward contract a portion of their crop for fall delivery. The average price for a flex lease payment could be the harvest delivery price at the local elevator, perhaps four times during the year: mid-January, mid-April, mid-July, or mid-October. Specific days of the month, such as July 15, should be established. The lease should note that if the designated day falls on a weekend, the trading day closest to that date will be used.

If a larger number of pricing periods is desired, choose one day monthly to collect the harvest bids. If both parties prefer to reflect a longer period of monthly averages, consider January through October. To avoid having to record this price every month, have the local grain merchandiser print out this average price at the conclusion of harvest. Also request that the merchandiser sign and date the information so that both the tenant and landowner are comfortable with the data source.

Establishing flexible lease payments

The flexible lease triggers for both corn and soybeans needs to be in your rental agreement. If you’re using the gross crop revenue from the farm, consider subtracting from this amount annually for each crop an estimate of total crop production costs including the base rent. These costs, once established in the lease, can adjust automatically each year. If the crop production costs appear to be too high or too low annually, then changes could be made to base rent, maximum rent, or how the base crop cost estimates are determined. For 2014, consider not triggering the flex payment until the gross crop revenue exceeds the base crop cost estimate for each crop. The following websites can provide additional information on flexible leases:

Illinois Cash Farm Lease

To use this lease form: Complete two identical copies—one for the Lessor (Landowner) and one for the Lessee (Tenant). Cross out any provisions that are not to become a part of the contract and add any additional provisions that are desired. If preparing the lease manually, use ink or typewriter; however, the web-based lease form can be filled in on-line before printing. This lease form is available on the farmdoc website at <http://www.farmdoc.uiuc.edu/legal/lease_forms_abs.html>. Additional leasing information can be found in the Leasing Fact Sheets prepared by University of Illinois Farm Business Management Educators located at <http://www.farmdoc.uiuc.edu/management/leasing_fact_sheets.html>. Note: A lease creates and alters legal rights; thus, Landowners and Tenants may want to discuss specific lease provisions with their respective legal advisors.

Date and names of parties. This lease is entered into on ________________________, 20____, between:

Lessor(s) (Insert Landowner’s exact name): ____________________________________________
whose mailing address is __________________________________________________________

and

Lessee(s) (Insert Tenant’s exact name): ______________________________________________
whose mailing address is __________________________________________________________

and whose Social Security Number or Employer Identification Number (if Tenant is an entity other than an individual) is ________________________________

The parties to this lease agree to the following provisions.

Section 1. Description of Rented Land and Length of Tenure

A. Description of Land. The Landowner (Lessor) rents and leases to the Tenant (Lessee), to occupy and to use for agricultural purposes only, the following real estate located in the County of _________________ and the State of _______________, and described as follows: ____________________________

__________________________________________________________________________

commonly known as the ______________________________ farm and consisting of approximately __________ acres, together with all buildings and improvements thereon belonging to the Lessor, except _____________________________.

B. Length of Tenure. The term of this lease shall be from __________, 20____, to __________, 20____, and the Lessee shall surrender possession at the end of this term or at the end of any extension thereof. Extensions must be in writing and attached to this lease, and both parties agree that failure to execute an extension at least ________ months before the end of the current term shall be constructive notice of intent to allow the lease to expire.

Section 2. Fixed Cash Rent (With Option for Indexing)

Tenant agrees to pay Landowner an annual fixed cash rent as identified below; however, if the “option for indexing” is also completed, the rent shall be adjusted as described in the option for the years following the first year.

Fixed Rent: The annual cash rent shall be the sum of $__________. This represents _______ acres of cropland at $_________ per acre, plus _______ acres of ________ at $________ per acre, plus _______.

Option for Indexing: After the first year, the annual cash rent for a particular lease year shall be the Fixed Rent identified above, but adjusted annually after the first year as follows:

__________________________________________________________________________

__________________________________________________________________________

Farmdoc Form: CL 01-0912. Form edited by D. L. Uchtmann, Professor of Agricultural Law, and Denney Ehrwald, Extension Educator. The editors express appreciation to other University of Illinois Extension Farm Business Management and Marketing Educators for their assistance with this form.
Section 2 (Alternate). Flexible Rent Using Option I, II, or III

CAUTION: “Flexible Rent” may cause a lease to be treated like a “share lease” under federal regulations (e.g., 7 CFR 1412.504) stating how government agricultural program payments can be divided between landlord and tenant. Consult with your legal advisor.

Note: Strike either Section 2 or Section 2 (Alternate). The cash rent can be flexible and change each crop year. A base rent can be established and adjusted based upon yield and/or price fluctuations. The factors to be used in adjusting the rent in Options I and II must be listed below.

<table>
<thead>
<tr>
<th>Crop(s)</th>
<th>Base cash rent (per acre)</th>
<th>Base yield (bu or ton/acre)</th>
<th>Base price (per bu or per ton)</th>
<th>Min. cash rent (per acre)</th>
<th>Max. cash rent (per acre)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
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</tbody>
</table>

The current price for the current year shall be the average price at close of day based on the following time period(s) and location(s):

<table>
<thead>
<tr>
<th>Crop(s)</th>
<th>Day</th>
<th>Month through</th>
<th>Day</th>
<th>Month at</th>
</tr>
</thead>
<tbody>
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</tbody>
</table>

A. For each lease year, the per-acre base cash rent for each crop shall be adjusted at the close of the cropping season by one of the following methods:

**OPTION I – FLEXING FOR PRICE ONLY**

<table>
<thead>
<tr>
<th>Crop(s)</th>
<th>Base rent x (Current price) Base price</th>
<th>=Rent/acre1</th>
<th>x Acres grown</th>
<th>= Adj. Rent for year</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$</td>
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<td>$</td>
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</tr>
</tbody>
</table>

**OPTION II – FLEXING FOR PRICE AND YIELD**

<table>
<thead>
<tr>
<th>Crop(s)</th>
<th>Base rent x (Current price) Base price</th>
<th>x (Current yield2)</th>
<th>=Rent/acre1</th>
<th>x Acres grown</th>
<th>= Adj. Rent for year</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
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</tbody>
</table>

**OPTION III – OTHER PROCEDURE TO BE USED**

B. Additional Rent for Inflexible items (complete at beginning of lease period)

<table>
<thead>
<tr>
<th>Item</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pasture</td>
<td>$</td>
</tr>
<tr>
<td>Hay land</td>
<td>$</td>
</tr>
<tr>
<td>Other inflexible cropland</td>
<td>$</td>
</tr>
<tr>
<td>Timber, wasteland</td>
<td>$</td>
</tr>
<tr>
<td>Farmstead</td>
<td>$</td>
</tr>
</tbody>
</table>

TOTAL INFLEXIBLE RENT $

C. TOTAL RENT FOR YEAR: Sum the Flexible cropland rent (calculated from Part A, Option I, II or III) and the Total Inflexible Rent (from Part B).

$
Section 3. Investments and Expenses

A. The Landlord agrees to furnish the property and to pay the items of expense listed below:

1. The above-described farm, including fixed improvements.
2. Materials for necessary repairs and improvements to buildings and permanent fences except as agreed to in B4 and amendments to this lease.
3. Skilled labor employed in making and repairing improvements and all labor for painting buildings.
4. Taxes on land, improvements, and personal property owned by the Lessor.
5. Fire and wind insurance, at a fair replacement value, on the residence and all buildings owned by the Lessor and used by the Lessee in storing or housing livestock, feed, livestock and equipment.
6. Ground limestone: Lessor is to furnish ______ percent or share of total cost, including hauling and spreading.
7. A water supply adequate for household use and ______ animal units of livestock.
8. Other items:

B. The Lessee agrees to furnish the property and to pay the items of expense listed below:

1. All the machinery, equipment, labor, fuel, and power necessary to farm the premises properly.
2. The hauling to the farm, except when otherwise agreed, of all material which the Lessor furnishes for making repairs and minor improvements, and the performing of labor, except skilled, required for such repairing and improving.
3. All seed, inoculation, disease-treatment materials, and fertilizers, except that which the Lessor agrees to furnish above.
4. The following described items and all other items of expense not furnished by the Lessor as provided in A:

Section 4. Tenant’s Duties in Operating Farm

The Tenant further agrees to perform and carry out the stipulations below. (Strike out any not desired.)

A. Activities required:

1. To cultivate the farm faithfully and in a timely, thorough, and businesslike manner.
2. To prevent noxious weeds from going to seed on said premises and to destroy the same and keep the weeds and grass cut.
3. To haul and spread all manure on appropriate fields at times and in quantities consistent with environmental protection requirements.
4. To keep open ditches, tile drains, tile outlets, grass waterways, and terraces in good repair.
5. To preserve established watercourses or ditches, and to refrain from any operation that will injure them.
6. To keep the building, fences (including hedges), and other improvements in good repair and condition as they are when the Tenant takes possession or in as good repair and condition as they may be put by the Lessor during the term of the lease – ordinary wear, loss by fire, or unavoidable destruction excepted.
7. To take proper care of all trees, vines, and shrubs, and to prevent injury to the same.
8. To keep the farmstead neat and orderly.
9. To prevent all unnecessary waste, or loss, or damage to the property of the Lessor.
10. To comply with pollution control and environmental protection requirements as required by local, state, and federal agencies, as well as to implement soil erosion control practices to comply with the soil loss standards mandated by local, state, and federal agencies.
11. To use prudence and care in transporting, storing, handling, and applying all fertilizers, pesticides, herbicides, and other chemicals and similar substances; to read and follow label instructions for the use of such materials in order to avoid injury or damages to persons or property or both on the leased premises and adjoining areas; and to comply with state pesticide training, licensing, storing, and usage.
12. Any chemicals for weed or insect control or other use, when used, should be applied at levels not to exceed the manufacturer’s recommendation for the soil types involved. The Tenant agrees to provide to the Lessor, annually, a written report indicating the product name, amount, date of application and location of application of all pesticides, fertilizers, and seed used on the farm.
13. No chemicals will be stored on the property for more than one year. When chemicals or petroleum products are stored on the farm, they will be only those planned to be used on the farm and they will be in closed, tight containers above ground and clearly marked. No chemicals or chemical containers will be disposed of on the property.
14. To generally follow Natural Resource Conservation Service and Farm Service Agency recommendations and to maintain all other requirements necessary to qualify current and future farm operators to participate in federal farm programs.
15. Other:

Page 3, Cash Lease – Farmdoc Form CL 01-0912
B. Activities restricted. The Tenant further agrees, unless the written consent of the Lessor has been obtained:

1. Not to assign this lease to any person or persons or sublet any part of the premises herein leased.
2. Not to erect or permit to be erected any structure or building or to incur any expense to the Lessor for such purposes.
3. Not to add electrical wiring, plumbing, or heating to any building. (If consent is given such additions must meet standards and requirements of power and insurance companies.)
4. Not to plow permanent pasture or meadowland.
5. Not to allow any stock on any tillable land except by annual agreement.
6. Not to burn or remove cornstalks, straw, or other crop residues grown upon the farm.
7. Not to cut live trees for sale purposes or personal uses.
8. Not to erect or permit to be erected any commercial advertising signs on the farm, other than seed variety signs.
9. Not to enter into any agreement, contract, or other farming or business arrangement that alters rights in the Lessor’s security interest, right of entry, default or possession.
10. Not to permit, encourage, or invite other persons to use any part or all of this property for any purpose or activity not directly related to its use for agricultural production, except as specifically noted here:

11. Other:

Section 5. Management and Business Procedures

The Lessor and Tenant agree that they will observe the following provisions (Strike out any not desired.)

A. General Cropping System. Except when mutually decided otherwise, the land use and cropping shall be as follows:

- acres for rotated crops
- acres in permanent pasture
- acres in non-grazed woodland
- acres in building and lots
- acres in other

B. Insurance. For the term of the lease, Tenant shall maintain insurance with a carrier acceptable to the Landlord, insuring Tenant while performing on these premises hereunder for the following types and in stated minimum amounts:

- Crop Insurance $________ per acre
- Liability Insurance: $________ per person
- Property Damage: $________ per occurrence
- Workers Compensation: As required by statute

Tenant shall furnish Landlord with a Certificate of Insurance and give notice of termination of coverage.

Tenant agrees that all applicable insurance policies name the Landlord as an additional insured

C. Financial and production records. The Tenant agrees to keep financial and production records of the farm business and to furnish an annual report to the Lessor, on such forms as the Lessor may provide, on or before

D. Cash Rent Installments. The cash rent shall be paid each year in the following installments:

<table>
<thead>
<tr>
<th>Dollars of percent of rent due</th>
<th>Date Due</th>
</tr>
</thead>
<tbody>
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<tr>
<td>Balance Due</td>
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</tr>
</tbody>
</table>

E. End of lease reimbursements. At the end of this lease, the Lessor agrees to reimburse the Tenant:

1. For the Tenant's remaining cost in limestone. The Tenant's remaining cost shall be calculated by depreciating the Tenant's net cost at the rate of ______ percent annually.

2. For the Tenant's cost of soluble phosphate (P2O5) and potash (K2O) fertilizers applied on crops harvested for grain in the last year of this lease minus the amount of these plant food elements, valued at the same rates, contained in the Tenant's share of these crops.

F. Land use in last year of lease. If, during the last six months of the lease term, or after notice to terminate has been given if this lease has become a year to year lease, the parties fail to agree on questions of land use, cropping system, fertilizer applications, or any deviations from the lease provisions, then the specific agreements in this lease shall prevail or, in the absence of agreements in the lease, the Lessor shall decide and the Tenant agrees to abide by the Lessor's decisions. The Lessor's decisions shall not contradict any provisions in this lease or violate good farming procedures.

G. Conservation. Both Lessor and Tenant affirm the goals of minimizing soil erosion losses and preserving the productivity of the land in ways that are consonant with their needs and desires for acceptable current returns to their individual inputs on the leased premises. To these ends they agree to implement as far as possible the best management practices recommended by the Natural Resource Conservation Service and to cooperate with that agency's soil and water conservation programs.

H. Tenant responsible for hired labor. The Tenant shall be solely responsible for all employer obligations on hired labor with respect to safety requirements and social security and workers' compensation contributions, and the Lessor shall have no responsibilities therefore.

I. Other management agreements:

Page 4, Cash Lease – Farmdoc Form CL 01-0912
Section 6. Default, Possession, Landlord's Lien, Right of Entry, Mineral Rights, Liability, Extent of Agreement

The Lessor and Tenant agree to the following provisions. (Strike out any not desired)

A. Termination upon default. If either party fails to carry out substantially the terms of this lease in due and proper time, the lease may be terminated by the other party by serving a written notice citing the instance(s) of default and specifying a termination date of ____ days from the date of such notice. Settlement shall then be made in accordance with the provisions of Clause B of this section, the reimbursement agreements of Section 5, and any amendments to this lease.

B. Yielding possession. The Tenant agrees at the expiration or termination of this lease to yield possession of the premises to the Lessor without further demand or notice, in as good order and condition as when they were entered upon by the Tenant, loss by fire, flood, or tornado, and ordinary wear excepted. If the Tenant fails to yield possession, the Tenant shall pay to the Lessor a penalty of $____ per day or the statutory double rent, whichever is less, for each day the Tenant remains in possession thereafter, in addition to any damages caused by the Tenant to the Lessor's land or improvements, and said payments shall not entitle the Tenant to any interest of any kind or character in or on the premises.

C. Landlord’s lien. The Landlord’s lien provided by statute on crops grown or growing, together with any other security agreement(s) created by Tenant in favor of Landlord, shall be the security for the rent herein specified and for the faithful performance of the terms of the lease. The Tenant shall provide the Lessor with the names of persons to whom the Tenant intends to sell crops grown on these premises at least 30 days prior to the sale of such crops. A lesser period may be allowed by mutual written agreement. Tenant consents to any filing required by law to perfect the statutory landlord’s lien upon crops. If the Tenant fails to pay the rent due or fails to keep any of the agreements of this lease, all costs and attorney fees of the Lessor in enforcing collection or performance shall be added to and become a part of the obligations payable by the Tenant.

D. Landowner's right of entry. The Lessor reserves the right personally or by agents, employees, or assigns to enter upon the premises at any reasonable time to view them, to work or make repairs or improvements thereon, to care for and dispose of the Lessor’s share of crops, to develop mineral resources as provided in Clause E below, or, after constructive notice has been given that the lease may not be extended, and following severance of crops, to plow and prepare a seed bed, apply fertilizers, and any other operation necessary to good farming by the succeeding operator, these operations not to interfere with the Tenant in carrying out the regular farming operations.

E. Mineral rights. Nothing in this lease shall confer upon the Tenant any right to minerals underlying the land. Such mineral rights are hereby reserved by the Lessor together with the full right to enter upon the premises and to bore, search, excavate, work, and remove the minerals, to deposit excavated rubbish, to pass over the premises with vehicles, and to lay down and work any railroad track or tracks, tank, pipelines, power lines, and structures as may be necessary or convenient for the above purpose. The Lessor agrees to reimburse the Tenant for any actual damage the Tenant may suffer for crops destroyed by these activities and to release the Tenant from obligation to continue farming this property when development of mineral resources interferes materially with the Tenant's opportunity to make a satisfactory return.

F. Landowner liability. The Tenant takes possession of the leased premises subject to the hazards of operating a farm, and assumes all risk of accidents personally as well as for family, employees, or agents in pursuance of farming operations, or in performing repairs on buildings, fences, tills, and other improvements.

G. Binding on heirs, etc. The terms of this lease shall be binding on the heirs, executors, administrators, and assigns of both Lessor and Tenant in like manner as upon the original parties.

Section 7. Additional Lease Provisions

Signatures of parties to lease:

__________________________  Landowner  ____________________________ Date

__________________________  Landowner  ____________________________ Date

By__________________________  Agent  ____________________________ Date

__________________________  Tenant  ____________________________ Date

__________________________  Tenant  ____________________________ Date

Page 5, Cash Lease – Farmdoc Form CL 01-0912
Amendments and Extensions to the Lease
(Must be completed manually/cannot be completed on-line)

**Amendments, alterations, and extensions** to this lease may be made in writing in the space below at any time by mutual agreement. The written amendments should be noted on both the Landlord’s and Tenant’s copies of the lease (complete and sign two identical copies). If the parties fail to agree on a proposed alteration, the existing provisions of the lease shall control operations.

**A. Improvements made by the Tenant at the Tenant’s own expense.** When the Lessor and Tenant agree that the Tenant may make all or part of an improvement (such as buildings, additions to buildings, major repairs, fences, bathrooms, water systems, etc.) to the farm at the Tenant’s own expense and that the Tenant is to be reimbursed for any costs remaining at the end of the lease, the necessary information shall be recorded in one of the following blanks and, after being duly signed by both parties, it shall become a part of the lease above and obligate the Lessor and his or her heirs and assigns to make such reimbursement. Such improvements become the Lessor’s property upon completion of the form below. The Lessor thereby assumes the responsibility for property taxes, insurance coverage, and risk of loss.

<table>
<thead>
<tr>
<th>Description and location of the improvement</th>
<th>Tenant’s net cost</th>
<th>Annual rate of depreciation (percent)</th>
<th>Date depreciation begins</th>
<th>Signatures and Date Signed</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td></td>
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</tr>
<tr>
<td>2.</td>
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<td>3.</td>
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</tbody>
</table>

**B. Lessor’s written consent to Tenant’s participation in items in Section 4, Clause B.**

1. Item: __________________ Description and restrictions: __________________________________________
   
   ___________________________ Date: ___________________ Lessor’s Signature ___________________________

2. Item: __________________ Description and restrictions: __________________________________________
   
   ___________________________ Date: ___________________ Lessor’s Signature ___________________________

**C. Other amendments:** To be dated, signed and attached to both Landowner’s and Tenant’s copies of lease.

**D. Lease Extensions**

<table>
<thead>
<tr>
<th>Lease Extension #1</th>
<th>Lease Extension #2</th>
<th>Lease Extension #3</th>
</tr>
</thead>
<tbody>
<tr>
<td>This lease, originally dated ___<strong>, 20</strong>, shall be extended...</td>
<td>This lease, originally dated ___<strong>, 20</strong>, shall be extended...</td>
<td>This lease, originally dated ___<strong>, 20</strong>, shall be extended...</td>
</tr>
<tr>
<td>From ___<strong>, 20</strong></td>
<td>From ___<strong>, 20</strong></td>
<td>From ___<strong>, 20</strong></td>
</tr>
<tr>
<td>To ___<strong>, 20</strong></td>
<td>To ___<strong>, 20</strong></td>
<td>To ___<strong>, 20</strong></td>
</tr>
<tr>
<td>Signed: ___<strong>, 20</strong></td>
<td>Signed: ___<strong>, 20</strong></td>
<td>Signed: ___<strong>, 20</strong></td>
</tr>
<tr>
<td>Lessor</td>
<td>Lessor</td>
<td>Lessor</td>
</tr>
<tr>
<td>Tenant</td>
<td>Tenant</td>
<td>Tenant</td>
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</tbody>
</table>