

SOUTHEAST NEBRASKA FARMLAND LEASING - 2017

What Is Your Most Important Decision?

WHO

Who Do You Want?

BEST

The first and most important leasing decision you make is WHO. After you have decided who the rest of your decisions are smaller in importance and if you did not select the BEST operator available you may have less than desirable success in the care and earnings of your investment the land. This may be what you want if a relative is involved, but you have to realize that it is very very hard to change operational style. So if it is not the best, it is not likely to suddenly become the best, but it may improve. Key Point #1 Fill In WHO and BEST.

FARMLAND EARNINGS

- Exciting when other investments are slow
- Long term investments
- Relatively safe investments
- Not Liquid
- Require Skill to Manage Well
- Earnings Are Approximately 6.5%
 - Cash After Taxes and Expenses 4%
 - Long term Asset Gain of Land Value 2.5%

Earnings on land are only exciting when the stock market and even the bond market are in the tank. Land is a long term investment. It is a relatively safe investment, but relatively hard to jump in and out of. Land asset value gain has been approximately 2.5% per year with three reversal periods since the 1930's. Skill and a genuine interest are required to manage your land asset well. A typical after tax and bill earning on land is 4% of land value. Example my land would have a value of about \$1050 per acre. I rent 151 of the 160 acres for \$75 per acre or earn a gross rent of \$11,325. The taxes were \$2725 and other expenses were \$1450. My earnings after tax were 4.27%. Key Point #2 mark 4% in cash and 2.5% in long term asset gain.

FARMLAND EARNINGS

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 - Cash After Taxes and Expenses 4%
 - Long term Asset Gain of Land Value 2.5%

Example

Good Dryland Bottomland Valued at \$4000/ A

Rent = (\$4000 x .04) + Taxes + Other Expenses

Rent = \$160 + \$36 + \$6 = \$204/ A

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FARMLAND RENT

- Rent Based on Crop Productivity
- Corn 5 Yr APH = 132
- Soybean 5 Yr APH = 47

Corn 132 X \$4.50 = \$594 Gross

Soybeans 47 X \$11.50 = \$541 Gross

Average Gross \$1135 Divided by 2 = \$568

Cash Rent Based on 30% of Gross = \$170/A

I have been using the average gross income and a 30% factor for dryland and 33% factor for irrigated with system owned by the landlord. My reasoning is this: If we had a net share lease 33% on dryland and 35% on irrigated would be fair shares. While cash rents are guaranteed, cash rents have also been quite aggressive. So I used a small discount. This method is very flexible for accounting for land of very different productivity.

RENTAL ARRANGEMENTS				
Lease Type	Landlord Risk	Tenant Risk	Landlord Reward	Tenant Reward
Cash	Lower	Higher	Lower	Higher
Share	Medium	Medium	Medium	Medium
Custom Farmed	Higher	Lower	Higher	Lower

The only risk the landlord has in a cash lease is getting the 2nd half of the payment and the harm a tenant may do to the land. Since risk is low reward usually will be slightly below other lease options. Share lease could be net share leases where the landlord only puts in the land and taxes, pays no share of annual production costs and gets a share of the crop equal to that share of input. This would be 33-35% of the crop for Southeast Nebraska dryland crops. If the landlord share is 40% then enough expenses are going to be shared to equal about 7% of expenses plus the 33% for land. 50% -17%, 60% - 27% etc. Purchasing all inputs and just having the farmer perform the operations for a set fee would be custom farming. It represents the greatest risk and the highest potential for income when averaged over a 10+ year period. Key Point #3 your greatest RISK and your greatest REWARD will come from your investment in the land.

RISK AND REWARD

Man Despite His Artistic Pretensions, His Sophistication, And His Many Accomplishments – Owes His Existence To A Six Inch Layer of Top Soil and The Fact That It Rains

My grandfather had this saying on his wall and I think it puts a solid and simple foundation on the way we should conduct ourselves in owning, managing, and operating our land resource.



A frequent question is how to consider rent for farm buildings like bins, lots, barns, etc.

Buildings, Lots and Bins

Depreciation	<i>D</i>	6.0 %		<i>F</i>
Interest	<i>I</i>	6.0 %		<i>I</i>
Repairs	<i>R</i>	1.0 %	1.0 %	<i>V</i>
Taxes	<i>T</i>	1.5 %	1.5 %	<i>E</i>
Insurance	<i>I</i>	<u>0.5 %</u>	<u>0.5 %</u>	
		15.0 %	3.0 %	

Key Point #4 is the DIRT I FIVE. The investment in grain bins or livestock barns has five main parts. D-Depreciation which is the slow deterioration of the building which is about 6% per year. I-Interest on the amount of your investment which is about 6%. R-Repairs on buildings amounts to about 1% per year. T-Taxes can vary by area, in Southeast Nebraska they amount to about 1.5% of building value per year. I-Insurance would be about 0.5%. Your desire is to get 15% of the building value per year. Prospective tenants start by suggesting 3.0% which would only cover yearly real expenses. If you don't get the RTI from me you will not get it from anyone. So 3% to 15% a wide bargaining range.

DIRTI FIVE EXAMPLE

Value of Grain Bin

New Well Equipped Bin Cost

\$1.80 Per Bushel for Large Bins (37,000 Bu +)

\$3.20 Per Bushel for Small Bins (10,000 Bu -)

Let's Use

\$1.55 per bushel for an Older Bins in Good Repair

Bins less than 8000 bu are of no real value

If we are going to use the DIRTI FIVE we need to value the building to be rented. I use \$1.25 per bushel for older bins with full aeration floors and fans in place. A bin construction company lists local costs of \$1.20 to \$1.75 depending on bin size.

DIRTI FIVE EXAMPLE

10,000 bu bin x \$1.55 per bu = \$15,500 Value

Full Price For The Year = \$15,500 x 15% = \$2325

Base Price to Cover RTI = \$15,500 x 3% = \$465

**Bargaining Settled at 8% +1% for electric = 9% =
\$1395/ year**

or = to \$.04 per bushel per mo. for 3.5 months

If we had a 10,000 bushel bin on the farm to be leased @ \$1.55 per bushel it would be worth \$15,500. The yearly lease would be \$2325 at 15% and \$465 at 3%. Our pricing bargaining arrives at 8% and adds 1% for electric use as the electric meter serves the entire farmstead not just the bins. So \$1395 per year which would equal about 3.5 months rent in commercial storage. A good choice for both landlord and tenant. The tenant isn't trying to get the bin empty as quick as possible to stop expenses and can even leave it in longer for market option choices. The landlord has a better chance of having the bin full during March to June tornado season and is able to recover part of their interest and depreciation.

Swine Buildings



<u>Building Type</u>	<u>*New</u>	<u>Serviceable</u>
Farrowing	\$1500	\$800
Gestation	\$650	\$400
Grower-Finisher	\$250	\$150
Nursery	\$140	\$80

* \$ per pig space

Farm Shop/Storage Buildings

<u>New Farm Storage Building</u>	<u>Used Reasonable Condition (80%)</u>
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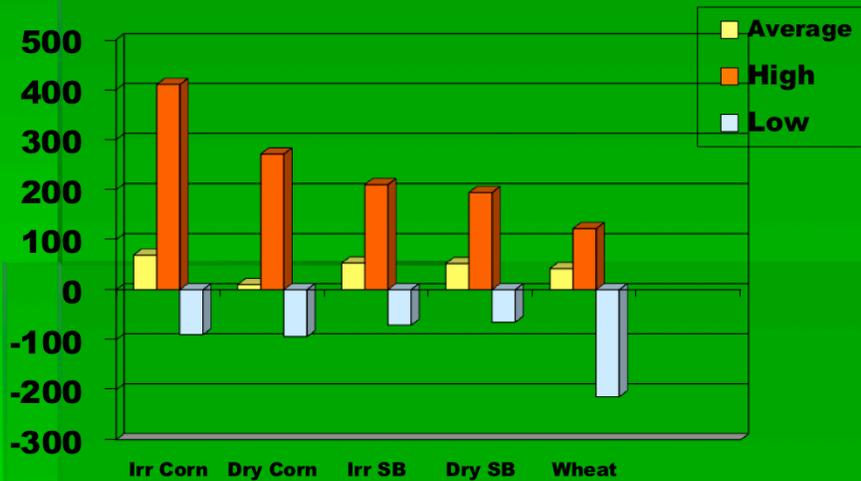
Rock Floor - \$8/ sq foot	\$6.40/sq foot
Concrete floor - \$15/ sq foot	\$12.00/sq foot

Examples - New

Rock 60 ft X 100 ft = \$48,000	\$38,400
Concrete 60 ft X 100 ft = \$90,000	\$72,000 (8% = \$5760 per yr)

Smaller building would have considerable less value or no value because of door sizes, space limitations and general usefulness.

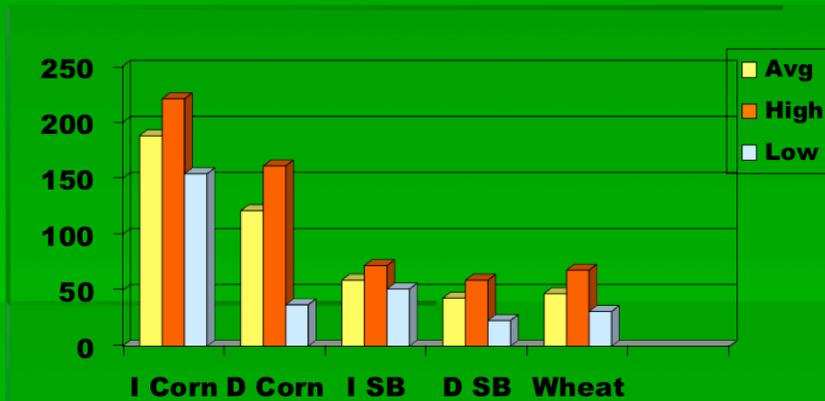
LONG TERM RETURNS ABOVE ALL COSTS NEBRASKA FARM BUSINESS ASSOCIATION – 20 year average



Production agriculture can be tight margin business. The average returns excepting government farm program payments is near zero with wide fluctuations in both the best and worst years. The five years from 2010-14 were the best in history. Significant downturn since 2015 is challenging managers.

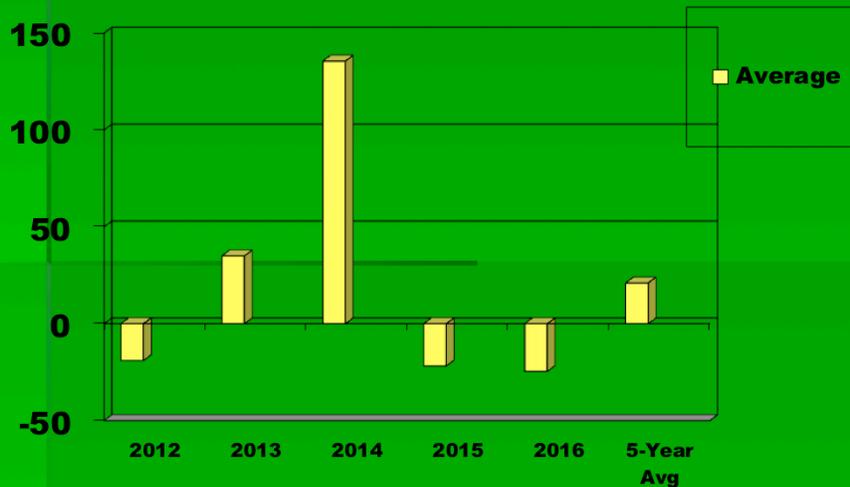
LONG TERM YIELDS

20 years of data



Yields also show a wide fluctuation. Note that the lowest yields are much closer to the average than the losses in those years were to the average. You do not have to drop yield very much to remove the profit. In the worst year some farmers are still making money. You could put some farmers on a iceberg and they would find a way to make money. Those are the WHO we should be seeking.

BEEF COW-CALF LONG TERM NET RETURN PER HUNDREDWEIGHT NEBRASKA FARM BUSINESS ASSOCIATION



Production agriculture can be tight margin business. The average returns excepting government farm program payments is near zero with wide fluctuations in both the best and worst years. The past five years have been the best in history. One can expect change.

Nebraska Farm Business Income, Expense & Net Trends

	'07	'08	'09	'10	'11	'12	'13	'14	'15	'16
Gross Income \$10000	62	78	87	92	103	128	126	101	99	101
Expense \$10000	55	60	62	66	77	88	87	88	85	90
Net Farm Income \$10000	20	20	18	28	41	37	17	18	3	4.5

Net farm income has to first pay taxes, second pay long-term principal payments, and third supply family living. There is a reason why 85% of farm spouses have an off farm job, and why nearly 35% of farm operators also have part-time off farm employment. Note the trend of rising cost of inputs which has really had a dramatic effect on net oncome in the post rally years 2013-2016. Net farm income broke the 4 year downturn in 2016 , but not by much.

LAND VALUES

UNIVERSITY OF NEBRASKA SURVEY

LEASE AVERAGES

UNIVERSITY OF NEBRASKA SURVEY

LOCAL SURVEY

6.5% OF LAND VALUE ESTIMATE

The University of Nebraska publishes yearly land value and rental rate updates available at Extension Offices or online at www.agecon.unl.edu . It is important to understand that there is a wide variation in land values and rental rates. A rule of thumb is that – Key Point #5 cash rent would be 6-8% of land value. Cash rent and pasture rent are paid only for the actual cropland or pasture acres, not the total acres. In Gage, Saline, Seward and Johnson Counties you can go to (Gage County Online) on the internet go to the assessors office and click on property tax valuations. You can find how your land and land in your area are assessed. Currently land is supposed to be assessed at 70% of actual value. Key Point # 6 the true value of the lease is the land, you need to protect and nurture it.



Tax, valuation and sale information is available on-line for many counties

<http://www.co.gage.ne.us/>

<http://www.co.johnson.ne.us/>

<http://www.nebraskataxesonline.us/> 05/04/2005

Crop Share Renting

Common Dryland Share Rent Arrangements

Net Share	67-33
Traditional	60-40
Aggressive	50-50
Reverse	40-60
Custom Farmed	30-70 or Cash \$90-100/A

Net Share lease would mean the landlord is putting in the land and taxes only.

What is Shared?

- Largest Landlord Share is Land & Taxes
- Need Fair Split
- Items Easily Divisible
- Items Regular and Usual
- Herbicide, Fertilizer, Insecticide Common
- Seed Not Usual, But Could Be Used To Replace Fertilizer

Crop Share Renting

Common Irrigated Share Rent Arrangements

Net Share	65-35
Traditional	50-50
Reverse	40-60
Custom Farmed	20-80 or Cash \$100-125/A

How To Get Paid

- Ask For A Prospectus
- Check References
- Get An Assignment
- Get Cash In Advance

Example: \$150 per acre cash lease

March & November @\$75. = \$150.00

March Only \$146.50

(8 months interest on \$75 discounted)

Getting paid has to always be a concern. You could ask possible tenants for a prospectus. A guide to how they farm, including acres, recent yields, bank references, services offered, farming methods, etc. Your attorney could get an assignment for the last half of the cash rent or the share rent, i.e. you would be in the same position as the bank or John Deere Credit Services, etc. I have sometimes argued if this is necessary you may have missed Key Point #1! Some cash rents have been paid up front. An example would be a \$150 cash lease paid \$75 in March and \$75 after harvest. Now paid up front as $\$75 + \$75 - (\$75 \times 0.07\% \text{ interest} / 8 \text{ months}) = \146.50

A Contract is A Contract

- A Hand Shake And A Written Lease
Both Are Contracts
One Terms Defined By Character
One Has Terms Defined By Language
- Written Lease Is Recommended
- For Family A Written Lease not Recommended
- **IT IS VITAL!**

Many landlords and tenants have questions when problems arise and say we really don't have a contract. This is not true. A handshake or oral agreement is a legally binding contract, though there may be some misunderstanding about what the terms are. The terms can be defined in court or better yet anything which is agreeable to both parties can be changed at any time. A written lease is recommended. If family members are involved a written lease is vital. Key Point # 7. I can site numerous stories both glad and unfortunately sad in terms of family effects on asset leasing.

LEASE BASICS TOP TEN

1. Written Lease Must Be Signed
2. Business Meetings Not Family Gatherings
3. Meet twice per year, At Signing, At Farm
4. Attorney Will Draw Up Most Leases For less than \$200
5. Lease Can Be Signed For Many Years

A written lease, usually a one year lease, needs to be signed each year. If it is not signed it becomes an oral lease loosely based on past tenets of the written lease.

Do lease signing and business at business meetings and not at family gathering. There is too much risk of misunderstanding and family discord during key family bonding times. Key Point # 8, keep it business.

I recommend that business meeting be conducted twice per year. Once at lease signing, usually in late February prior to March 1 and once in late August or early September pre-harvest at the farm to discuss the crop and updates that must be addressed in the winter or future years.

Most farmland and/or building leases can be drawn up by your attorney for about \$100 to 125. The same lease can be signed and be updated with signed adjustments for many years.

LEASE BASICS TOP TEN

6. Oral Leases And August 31
7. Phosphorus and Lime Five Year Rule
8. With Family Make Sure It Is Just Family
9. If Details Bother You - Hire A Land Manager
10. Expect Land Manager To Earn Their Salt

When the terms of oral leases are debated in court, the court would generally say that if the tenant is not notified in writing before August 31 of this year then they have the lease for next year. This protects the tenants interest in wheat and post harvest fertilizer and other preparations for next year's crop. Again anything which can be agreed on can be changed at any time.

Lime and manure applications containing multiple years of phosphorus fertility can be worrisome whether the expense is shared or all the tenants cost. It is helpful to write a little 5 year agreement to protect the tenants interest in case the lease is changed in the next five years. For example the liming cost \$50 per acre and in this case the tenant bore all the cost. After three years, the landlord sells the property and pays the tenant 2/5 or \$20 per acre for the long term lime investment. The \$20 would usually be recovered from the new tenant or in the sale price of the land.

Discussions of leases and inheritance issues and future plans are best kept to the immediate family. Let your children share the info with the in-laws when they get home.

Land requires interest and effort. To protect your investment if you have little interest then either sell it or hire a land manager. If you do hire a manager they earn 10% of gross, so make them earn their salt.

LEASE CONSIDERATIONS

Highest Quality Tenant

Supports Your Interest in Increasing Land Value

Farm is Properly enrolled in USDA Programs

Maintains all Educational & Regulatory Permits

Uses USDA, State, NRD, & Private Cost Share

Cuts and Treats Trees in Fencerows

Key Point # 10 is for the tenant to help you increase profits and share those increases with you as per your arrangement. As we saw in a previous slide USDA programs represent a very important part of production agricultural income and insurance coverage. Add to that from 1 to 8 licenses and permits required for various operations. It could badly damage your property value to have livestock lots closed or herbicide spills or illegal dump sites traced to your property. Cost share opportunities can both increase the speed at which conservation improvements can be made and can also reduce costs.



Rent is only paid on cropland acres. As the fence row expands the crop acres diminish.



Can the combine get by these trees? How much yield reduction would you expect 30 feet out from tree competition?



Again trees are in the way, but wait maybe you would like to use this property for hunting and your wife enjoys bird watching. We could put a 20-30 foot buffer of native grass to this tree line and enjoy the Baltimore orioles nesting in the tree. The income from the buffer could come from CRP and we might also be about to lease hunting rights. Make sure your wishes are communicated to the tenant and again combine your wishes for the best profit for both of you.

LEASE CONSIDERATIONS

Terraces Maintained at Proper Height

Terrace Ends Repaired

Roadsides Mowed – County/Township Require

Waterways Mowed and Maintained

Produce Top Yields

Land Farmed Using No-Till

Southeast Nebraska soils are low water intake rate soils. Combine that with bare soils and heavy summer rains and you have gullies and Mississippi River Delta fill instead of productive Nebraska cropland. Terraces, Contour farming and no-till are very important.



This tenant is doing a great job of farming on the contour, maintaining terraces and no-tilling.



This tenant has fixed the terrace end as part of taking care of details. The next step should to start cover crops on these repair spots to begin the healing process immediately.



This tenant has let this waterway erode and become infested with trees.



There are several concerns here. This tenant has nearly destroyed this waterway. A ditch is opening to the fore right. Just why is this tenant having so many ins and outs. Is there a trash dump on your land? Is there a meth lab or marijuana growing operation back over the rise?



This water way has been mowed, but even here a hole has developed. Waterways require quite a bit of maintenance which is one of the reasons more land is moving to tile outlet terrace systems..



Several Counties require or request that land owners/operators mow the roadsides. This one is done quite nicely.



This roadside has not been cared for and seven young locust trees are growing in the grass between here and the trees. It will not be long before routine mowing is replaced by expensive bulldozer costs.



Quality tenant has no-tilled for the past 8 years. Great soil protective cover.



High yielding milo provides good habitat, soil protection, and a great place to start the next soybean crop using no-till methods.



Excellent soil cover.



Corn planted into standing wheat stubble will out yield this field by 25-28 bushels per acre. Over \$90 in lost income and soil erosion making sure the future doesn't get any better.



The first rain will destroy this exposed surface soil and cut and wash.

LEASE CONSIDERATIONS

Control Troublesome Weeds

1. Reduced Yield
2. Prohibited Noxious
3. Added Cost
4. Land Value

Lack of good weed control costs money in both share leases and cash leases.



This landlord has a visible sign of poor weed control! Cockleburs are one of the most costly yield robbers.

LEASE CONSIDERATIONS

Tile Outlet Terrace System

Cleaning Risers

Back Filling Along Line or Around Risers

Keeping Diaphragms In Place

Resetting Risers Downed By Cattle/Equip

Outlets Are on Grassed Waterway

Tile Outlet terrace systems need to be designed well and need maintenance attention. Taking out backflow diaphragms can risk the loss of the entire system during heavy storm events. A past incidence saw a 6-7 inch rain in an hour creat an 8 foot water sprout in the second terrace down and it washed out the terraces and the line all the way to the bottom of the hill.

LEASE CONSIDERATIONS

Maintain Field Drives

Decommission Open Wells With Cost Share

Protect Gas Line Markers and Lines

Clean Up Trash

Consider Hunting Rights Value

Properly Post and Protect Property

Crushing road tile ends, leaving open pipes to the underground water supply, wells baring gas lines, and allowing trash to have babies is not the way to protect your investment in land.



Well maintained tube.



NRD cost share is available of decommission wells. Get the tenant to help get the tower down and you will both be winners.



Gas markers have to be avoided and soil shaping on terraces and even in livestock lots have to be designed to maintain proper gas line cover.



Parent trash pile, if left it just attracts more.



This must be the baby.



Here the tenant has dumped trash on the field for an unknown reason.



Keeping trespasses off is usually wise. Generally speaking posting leased for hunting signs is more effective than keep out or no hunting. Don't be surprised is someone entirely unknown to you our your tenant is outraged as they feel they have a right to your land and its wildlife.



Drive access closed for winter.

IRRIGATED LAND LEASES

Irrigation Engine Oil & Filters Changed

No Engine Oil Dumping

Pivot Tracks Filled & Rocked As Needed

Winter Water Drained – Sand Trap Cleaned

Drain Water in Gear Boxes

Alignment Control Adjusted

Check U-Joints, Gearboxes, Tires

Protecting and caring for irrigation equipment is vitally important to protect the investment.



This no till tenant has filled the pivot tracks.



This pivot track is filled in the field, but is deepening the track through the waterways.



This landlord paid for the rock which the tenant placed in the track lines.

PASTURE CONSIDERATIONS

Highest Quality Tenant

Weed Control – Both Annual & Perennial

Fertilization at Proper Time

Cutting and Treating Trees, i.e. Hedge, Locust

Repair Gates and Fences

Care of Corrals and Buildings

Erosion Controls to Prevent Gullies

Pasture land also requires maintenance attention.



This tenant is not controlling the trees and is over grazing this pasture.



This CRP is not very useable for emergency hay harvest which means increased cost and lower returns.



Well maintained and poorly maintained fence in the same line.

PASTURE CONSIDERATIONS

Proper Grazing Management

Repair and Maintenance on Water Sources

Wells

Ponds

Dugouts

Tree Control

There are some good water development cost share options.



Look about $\frac{3}{4}$ of the way to the telephone pole. There is a small cedar down in the grass. Not much to worry about.



It has gotten a bit worse.



Well a few more.



There ought to be a government program to overcome my lack of interest in caring for my land!

QUESTIONS



Paul C Hay, Extension Educator
1115 West Scott Street
Beatrice NE 68310

(402) 223-1384
Fax: (402) 223-1370

Email: phay1@unl.edu
Website: www.gage.unl.edu

Don't hesitate to drop me an e-mail with your thought positive or negative and any questions.