**Checklist of Leasing Considerations**

Draft

**General procedures for establishing an equitable lease arrangement:**

* Use the cost contributions approach to establishing an equitable crop share, cash, or flexible lease arrangement.
	+ Share revenue in the same percentage as you share costs in the production process.
		- Must estimate the cost contributions of each party for the type of lease desired.
		- End result may deviate from the cost contributions final estimated shared revenue if the lease is a cash or flexible cash lease rather than a *share lease*.
		- The estimated cost share split is a good place to start when establishing a cash lease.
* ***Use a written lease*** to protect and maintain good relationships between all parties.

**Provision a lease (a binding contract) should contain:**

* Starting and ending dates
* Renewal and termination provisions
* Adequate description of the property including land and improvements
	+ Including maps and/or other documents that detail physical boundaries and operational characteristics such as government programs, if desired.
* Specify production inputs, management and marketing to be provided by each party
	+ Encourage the most profitable operation
	+ How, when, and where each party will share in income and expenses
		- From primary enterprises (small grains, hay, cow-calf)
		- From secondary enterprises (aftermath grazing, straw)
* Specify how participation in and resulting benefits of government programs are handled between all parties for all crops and livestock enterprises on the operation.
* Specify responsibilities of each party
* Establish farming/ranching practices to be used
	+ Tillage systems and crop rotations; organic or non-organic
	+ Livestock stocking rates and associated grazing practices such as buffer zones
	+ Habitat for wildlife or other conserving use
* Provide for control and use of non-farming/ranching related use rights.
	+ Hunting, fishing, agro-tourism, or…
	+ Who and how is additional liability with this activity covered
* Provide for new or needed capital improvements
	+ Provide reimbursement to the tenant for unexhausted capital improvements
	+ Provide for making capital improvements in lieu of rent
	+ Caution in using tax depreciation methods for determining improvement life
* Provide terms for assignment and subleasing options of:
	+ Farming and ranching related resources
	+ Possible uses of buildings and improvements for other activities
* Provide terms for the death of one of the parties

**Provision a lease (a binding contract) should contain: (continued)**

* Encourage the optimum productive use of capital while maintaining the long term health of the resource.
* Established in a way that handles “material participation” for social security and “special use valuation” for estate tax purposes that meets the IRS test, as desired by all parties
* Provide legal protection for all parties for potential problem issues

**Are you *average* and what does average look like for tenants?**

Does a 1/3 – 2/3 “traditional” crop share split reflect your situation? Many landlords and tenants rely on traditional lease arrangements to establish lease rates. These traditional split percentages were established form a history of lease arrangements among many different parties over a long period of time. While using these traditional split percentages is convenient, you must ask “is my operation and the way I farm really representative of these traditional splits?” If the answer is no, do not depend on traditional agreements to provide the correct compensation in a lease agreement.

**1**

**2**

**3**

**4**

Figure 1. Examples of four normal distributions.

**B**

**A**

Figure 1 provides an illustration of four normal distributions that are very different from each other. When you accept a traditional (normal) lease arrangement, what does that really mean for the possible profitability outcomes for a particular lease?

Several operational characteristics may make choosing a traditional 2/3 percentage split for the tenant a bad move. These would include an investment in a machinery and equipment compliment that is above the average, distribution #2 rather than distribution #1. Higher operating input costs due to poorer soil, point B on distribution #3 rather than point A. Greater variability in yield potential due to geographic location resulting in distribution #4 rather than distribution #3.

**Sources of information (publications, forms, software)**

* http://www.montana.edu/softwaredownloads/