## Introduction

Welcome to the New England Farm Leasing online tutorial.

The tutorial was developed as part of a project called ***Understanding and Negotiating Leases for New England Farm Entrants***.

The goal of this tutorial is to introduce you to the benefits and challenges of leasing. It will explain types of farm leases, and when to use them. It may help you consider, design and negotiate legally sound, written lease agreements.

While this tutorial and the project are intended for aspiring, new and beginning farmers, anyone interested in farm leasing will find useful information in these modules.

By completing the tutorial ***you are eligible for technical assistance*** from service providers familiar with farm leasing. For example, we will review your draft lease, check on a legal question, or help you think through a lease-related decision.

The tutorial is organized into four modules:



Each module contains an introduction, pertinent information on the topic, resources, and a self-test to help you review your learning.

This tutorial was development by Bob Bernstein and Kathy Ruhf, (Land For Good, Inc.), Debra Heleba (University of Vermont Extension) and Annette Higby, Attorney at Law, Randolph, Vermont as part of a project funded by the USDA/CSREES Northeast Center for Risk Management Education.

Please contact Land For Good at info@landforgood.org and/or 603-357-1600 if you have questions and/or feedback about the tutorial.

PLEASE ENTER YOUR NAME AND EMAIL ADDRESS HERE:

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## Module 1

# To Lease or Not to Lease—Making the Decision

In this module, you will explore the pros and cons of leasing as a farmland tenure strategy.

## Introduction

Tenure means "to hold." There are two basic ways to hold land: ownership or tenancy. A tenant does not hold title to the land, but has certain use rights that are specified in a rental agreement (a lease). Consider four essential components of farmland tenure:

1. ***Access:*** the right to occupy and use the land
2. ***Security****:* assurance that you can stay on the land
3. ***Equity****:* expectation that you can get a return on your investments in the property
4. ***Clarity:*** articulation of reasonable division of rights and responsibilities

A lease is defined as "an oral or written agreement (a contract) between two people concerning the use by one of the property of the other." (Nolo www.nolo.com/glossary.cfm)

In New England, approximately 30% of farmers rent some or all of their land (2007 Ag Census). Nationally, the figure is closer to half, and, despite a historic cultural bias toward property – and farm – ownership, this proportion of farm tenancy has been the case for generations. And because of the recent dramatic rise in land values, the trend toward leasing farmland is likely to increase.

A good lease can offer flexibility and affordability for a farmer's business. But leasing is NOT for everyone. Before you enter a lease agreement, review the information below as well as Modules 2 through 4 to become more familiar with lease agreements.

## Advantages of Leasing

- ***Excellent way to get started****.* As a new or beginning farmer, leasing can be an excellent strategy to test your farming skills as well as becoming acquainted with the particular piece of land without making the investment in buying it. If you discover that farming is not for you after all, or that the piece of land is not suited to the type of farming you want to pursue, you have the flexibility to move on without the burden of owning the real estate.

- ***Available land***. Throughout New England, land prices have been steadily rising while residential and commercial development have reduced the amount of available farmland, so finding an affordable farm to buy can be a serious challenge to farmers. More and more non-farming landowners and retiring farmers have farmland that they do not want to sell, but would consider leasing to a farmer.

- ***Wise use of capital****.* For many start-up farmers, initial investment should be focused on building the business instead buying real estate. Often new and beginning farmers think that their first step should be to purchase land. They end up frustrated when their farming career idles while they search for that “perfect” farm. You can jumpstart your farming career by leasing land, investing your dollars into building a successful business.

- ***Affordability.*** Renting land can be cheaper than owning. The financial benefits of leasing versus owning include: a) the ability to take tax deductions for leasing costs; and b) don’t have to pay property taxes and other costs associated with owning real estate.

## Disadvantages of Leasing

- ***No ownership of farmland***. Although leasing gives you access to farmland and can provide secure tenure, it does not allow you to own farmland. For many new farmers eager to have their own place, farming is equated with owning—some simply feel they must own land to farm it. The reality is that many farmers across New England both own and lease farmland. However, if you are not willing to farm without owning land, leasing is not for you. Also, while some longer-term leases can serve as collateral, you don’t own land to borrow capital against.

- ***Insecure tenure***. Leasing can be an insecure form of tenure. Because you do not own the land, and especially if you have a short-term lease and/or no written lease, leasing can leave your farming operation vulnerable to your landlord’s changing priorities or situation.

- ***Limited investment***. A tenant is much less likely to make investments in leased property, especially with a short-term lease, where you might not see the return on your investment during the life of the lease.

- ***Requires a relationship****.* Successful leasing requires effective communication on the part of both parties. If you are not willing to discuss issues and negotiate with a landowner, then leasing will likely be difficult.

- ***Poor or few opportunities*** *in your area*. Poor quality land—soils that are too wet or infertile—and insufficient access to the land are reasons not to lease that land. Consider NOT leasing a parcel if you will need to invest a considerable amount of money in soil fertility, particularly if you cannot recuperate those costs within the term of the lease agreement.

**GO TO THE NEXT PAGE FOR YOUR SELF-TEST**

## Self-Test

*Instructions: On a sheet of paper, write your answers to the following questions. Then check your answer to each question by clicking on the question below.*

1. What are the basic ways to hold land?
2. What are the four essential elements of land tenure?
3. What is a lease?
4. What are three advantages to leasing?
5. What are three disadvantages of leasing?

## Literature Cited and Further Reading

## Resources

- Lease Agreement Guide for Landowners and Farmers
- Managing Landlord-Tenant Relationships: A Strategic Perspective
- Farm Rental Agreement Checklist
- Farmland Tenure and Leasing, from A Legal Guide to the Business of Farming, UVM Center for Sustainable Agriculture
- *Holding Ground: A Guide to Northeast Farmland Tenure and Stewardship*, Available for purchase at http://www.smallfarm.org/bookstore/
- *A New Lease on Farmland* available at www.smallisbeautiful.org
- Sample Short-term Lease
- Sample Long-term Lease on Public Land
- Family Farm Series Publications: Farm Management

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## Module 2

# Types of Leases

In this module, you will learn about the different types of leases, their advantages and disadvantages, types of landlords, and lease payment options.

## Types of Leases

Leases can be categorized in three ways:

1) What is being leased;
2) Term (length); and
3) Payment options.

**What is being leased*:*** Most often, farmers think about leasing crop or pasture land. However, farm buildings, equipment and livestock can also be leased. Many people – including farmers -- rent (lease) their housing. A residential lease is typically written separately.

**Term*:*** Most farm leases are short-term – one to three year periods. Longer-term leases can be 5, 10, 20 and up to 99 years. Both short- and long-term leases have similar basic provisions. However, long-term leases usually contain more provisions. In any case, it is always recommended to have the agreement in writing.

**Payment options*:*** There are several ways tenants and landlords can arrange payment. The most common payment formula is a straight cash lease. Other arrangements such as flexible cash, crop-share or livestock-share or lease-purchase are less common but offer some advantages. (See below for more detail on these payment options.

## Types of Landlords

There are three basic categories of landlords:

1) Private, individual/family landowners;
2) Public landowners; and
3) Organizational landowners.

**Private, individual or family**: Traditionally, farmers rent land from other farmers or from individual or family landlords who are not farmers. In fact, nationally 88% of farmland landlords are *not* farm operators. The trend toward non-farming landlords is increasing. While often called absentee landlords, some of these landowners live on or next to the rental property.

**Public landholders** include municipal, state, and federal lands. Examples include town-owned open space, state park or institution (e.g., corrections or mental hospital) facilities, and federal parkland.

**Organizational landowners** include conservation land trusts, community land trusts, intentional communities, residential developments, Community Supported Agriculture farms, and religious orders.

A variation on these occurs when more than one entity has a legal stake in the property. For example, privately held land may have a conservation easement held by a land trust. Both parties may influence the terms of a lease with a farmer.

## Short-term Leases

***Characteristics:***

- Typically annual; can be one to three years
- Often verbal (not written down and signed), although written is always recommended
- Embedded in local farm culture; rental parcels can be rotated among farmers

***Advantages for farmer***:

- Can have lower costs than purchasing
- Offers ability to test enterprises, location, markets without long-term commitment
- Can take advantage of tax deductions for lease costs
- Typically simple to draft and negotiate
- Can be renewed; can have rolling term that provides some more security
- Allows tenant and landlord to built relationship that may result in longer-term agreement
- May be used as a tool to transfer ownership of farm assets

***Disadvantages for farmer:***

- Lack of security – can lose the land
- Cannot benefit from appreciation of land or recover lease costs as equity in land
- Lease costs can drain net income
- Limited control over the land
- May not be able to get credit
- May lose investments in land or infrastructure
- Less incentive to make longer-term conservation investments in the land

## Long-term Leases

***Characteristics:***

- Term can be anywhere from a few years (3 or 5) to 99 years

- May separate out ownership of improvements on the leased land (see ground lease, below)
- Detailed, written lease document
- Maintenance, repair and improvements are addressed in more detail
- Lease term may be limited by state law (e.g., no longer than 5 years)

***Advantages for farmer:***

- Maximum security without ownership
- Lengthens planning horizon
- Allows longer-term business and conservation planning
- May allow capture of investment in land and structures
- May increase borrowing capacity
- Can serve as legacy if lease is renewable and inheritable

***Disadvantages for farmer:***

- Reduces net income without contributing to long-term accumulation of wealth in property
- May entail more stakeholders, complexity and higher legal costs
- Greater investment may make it more complicated to terminate earlier
- Lease may not be sufficient to lenders

## Ground Leases

***Characteristics:***

- Typically executed with community values framework – land preservation, farm affordability, etc.
- A long-term lease for land only
- House, farm structures (existing and new) are separated and owned by tenant
- May include perpetual affordability clause which keeps the leased land and the improvements affordable for future tenants/owners
- May include active agriculture clause requiring that the land be in active farming use

***Advantages for farmer:***

- Maximum security without ownership
- Ability to build equity in improvements
- Lengthens planning horizon
- Allows longer-term business and conservation planning
- May increase borrowing capacity

- Can serve as legacy because lease can be renewable and inheritable

***Disadvantages for farmer:***

- Still don't own the land
- May entail more stakeholders, complexity and higher legal costs
- Can be challenging to negotiate rights and responsibilities
- Affordability provisions limit return upon sale to the next farmer
- Greater investment may make it more complicated to terminate earlier
- May be difficult (but not impossible) to secure a loan

## Lease Purchase or Leases with Option to Purchase:

***Characteristics:***

- Lease Purchase – agreement that tenant will purchase the leased asset at a point in the future
- Lease with Option – agreement that tenant has option to purchase the leased asset in the future
- This option can be used for land, buildings, equipment and livestock

***Advantages for the farmer:***

- Guarantee that the land (or other leased asset) will be available to the farmer
- Terms of the purchase are specified in the lease; in some cases this includes the price
- Allows tenant to postpone purchasing and save for purchase
- Timing is flexible

***Disadvantages for the farmer:***

- Tenant may wind up with an obsolete or worn-out asset
- Tenant does not benefit from depreciation expense
- Lease fee (rent) does not go toward purchase price unless specified

## Leasing Farm Buildings

Farm building leases are less common in New England (unless the building is part of the whole leased farm). Leasing farm buildings makes it possible for the tenant who lacks capital to invest, obtain use of, and generate farm income through the use of those buildings and facilities. One challenge is determining the rental rate for the building. There are various approaches – based on owner's costs, market rate, building capacity (e.g., per stall) or tenant's cost of production.

A lease for buildings should be written.  It typically contains the same basic provisions as a land lease.

## Residential leases

In some cases, a farmhouse or living unit is made available for rent along with farmland.  The residence and land can be combined in a single lease, although often a separate rental agreement is recommended for the residence.  There is a whole set of laws and regulations about rental housing, and several templates are available online.  Sometimes the residence and the land are tied together through a legal instrument.

## Payment Options

- ***Cash lease:*** a cash lease is the most straightforward.  The amount of rent is set, and the tenant pays the landlord a cash payment by a certain date.  The rent must be paid regardless of conditions.  This is the lowest-risk approach. Sometimes, rent may include an in kind component such as the tenant providing a certain amount of labor (e.g., keeping trails clear) in lieu of some cash.  Some landlords will accept a lower rental rate in order to provide an opportunity to new farmers, or for other social values.

- ***Share lease:*** A crop or livestock share lease is based on the proposition that the landlord and tenant share risk and reward, so there is less risk for the tenant, and less requirement for operating capital.  They split expenses and profits according to an agreed-upon formula.  Typically the landlord contributes land; other inputs could include management, and the tenant contributes labor.

***Flexible cash lease***:  A flexible cash lease is a hybrid between a cash and share lease.  A base rent is set based on expected production, and the landlord receives a share of any additional profit.  It reduces risk for the tenant and rewards the landlord in good years.

**GO TO THE NEXT PAGE FOR YOUR SELF-TEST**

## Self test

*Instructions: On a sheet of paper, write your answers to the following questions.  Then check your answer to each question by clicking on the question below.*

1. What are three ways to categorize leases?

2. What are the three types of landlords?

3. What are two advantages and two disadvantages of short-term leases?

4. What are two advantages and two disadvantages of long-term leases?

5. What are two advantages and two disadvantages of ground leases?

1. What are three common lease payment options?

## Resources

- Lease Agreement Guide for Landowners and Farmers
- Managing Landlord-Tenant Relationships: A Strategic Perspective
- Farm Rental Agreement Checklist
- Farmland Tenure and Leasing, from A Legal Guide to the Business of Farming, UVM Center for Sustainable Agriculture
- *Holding Ground: A Guide to Northeast Farmland Tenure and Stewardship*, Available for purchase at http://www.smallfarm.org/bookstore/
- *A New Lease on Farmland* available at www.smallisbeautiful.org
- Sample Short-term Lease
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## Module 3

# What's in a Lease?

In this module, you will learn the basic information included in most lease agreements.

## Introduction

A lease agreement serves several purposes. First, a written lease is a legally binding contract that entitles your farm business to access and use of the property. Second, it can be used as a communication vehicle between the farmland owner and the farmer tenant—a place where decisions about who is responsible for what, why and when are recorded. Third, it serves a role in the management of your farm business as a document useful for lenders and other service providers.

At minimum, every lease agreement document should include the following:

1) ***A description*** of the property and parties involved;
2) ***The time period*** in which the lease starts and ends;
3) ***The kind and amount of payment***; and
4) ***Signatures*** of both parties.

Within these parameters, a written agreement could be as informal as a letter including the above (remember to have both parties sign!) and as formal as a multiple-page, in-depth lease agreement drawn up by an attorney. It is important to get the agreement in writing as handshake or oral agreements can be misunderstood by own or both of the parties and may not hold up in court.

The following describe sections commonly included in lease agreements. Depending on the laws of the state in which the property is located, additional specific information may be necessary. To ensure that your lease includes this information, it is always recommended that an attorney review your lease agreement.

## 1. Descriptive Information—The Who and What

Typically, a lease starts with a description of the property and the people involved.

- **Description of Property**. Start with describing the land, farm structures, and residence that are to be included within the lease agreement. Note the current condition that serves a s a baseline to assess improvements or deterioration down the road. Photos can help.

- **Contact Information of Parties Involved**. In this section, the names of each party, along with their current phone, email and mailing addresses, are included. Be sure to specify whether the landowner is an individual or a legal entity (like a partnership, LLC, trust, etc.). Also specify if you or your business (if it is formed under a legal entity) is the contact.

## 2. Terms

At minimum, the terms section of the lease should include the following:

- ***Dates***. The dates that the lease starts and ends.
- ***Payment***. The kind, amount, time and place of payment. (See Module 4 for more information on rental rates.)
- ***Renewal***. A description of any rights to extend or renew the lease. Is the lease renewable? What is the procedure for renewing the lease? Is renewal automatic? Do both parties have the option to renew or not renew?
- ***Termination***. How the lease can be terminated by either party. For example, will the lease terminate on a specific date or will it end at the will of one or either party? If terminable "at will," how much advance notice needs to be given? What actions by either party will constitute a default under the lease? Will the non-defaulting party have the right to terminate the lease or withhold rent until the default is cured? Will the lease spell out a process to resolve disputes?

## 3. Permitted and Prohibited Uses

Descriptions of allowable and prohibited uses of the farmland are included in this section of the lease agreement.

- ***Permitted uses*** may be as broad as "agricultural activities" or specify a certain type of farming. Permitted uses might include harvesting cordwood, erecting agricultural structures, storing farm equipment, drawing water from the stream, etc.
- ***Prohibited uses*** should be clearly spelled out. These could include removing trees, using chemical inputs, placing structures in certain areas, storing fuel, raising hogs, public access, etc.
- ***Rights of entry*** for landlord, usually with prior notification. This does imply that the landlord can intrude on your business or home, but it does mean that s/he has a reasonable right to inspect the leasehold for compliance.
- ***Stewardship*** issues are often included in this section. This might be anything from requiring an NRCS conservation plan with annual review, to a specific management approach for the woods, strategies for habitat enhancement or soil improvement, and the like.

## 4. Maintenance, Repairs and Improvements

A common misunderstanding between farmland owners and farmer-tenants is what constitutes maintenance, repairs and capital improvements. A good lease agreement should clearly specify who is responsible for what, and how decisions about repairs and improvements are handled between the parties.

***Maintenance and repairs*** keep land and buildings in proper condition -- that maintain upkeep of normal and tear of buildings and land. Examples of routine maintenance and repairs include:

keeping culverts open, fixing road wash-outs, fixing broken windows, replacing a missing shingle, fixing a leaky pipe.  These are typically the responsibility of the tenant.

***Major repairs***, replacement, and rehabilitation like re-roofing the shed or replacing a well typically are the responsibility of the landowner.

***Capital improvements*** are changes or additions to land and/or buildings. Examples of capital improvements include the construction of a new greenhouse, installing permanent fencing, addition of electrical wiring and plumbing and other renovations to existing buildings, etc. Capital improvements also include such conservation installations as drainage tile.

Depending on the agreement, the tenant or landlord – or both – are responsible for these types of activities.  The tenant should always receive written permission from the landowner before making capital improvements.  Typically, the landowner retains the improvements at the termination of the lease.  Under the right circumstances, making a capital improvement on someone else's land can be a sound option.  He could own and sell it to the landlord or the next tenant, or depreciate it over the life of the lease.   If a lease is terminated prematurely, there are mechanisms to protect the tenant's investment.  For example, the tenant could be allowed to remove the improvement, or the landlord could pay the tenant for its undepreciated value.

## 5. Insurance and Liability

The lease should specify insurance requirements.  Most often, landlords will (or should) require evidence of the tenant's liability insurance, naming the landlord as additional insured.  This is not an extravagant expense, and a savvy farmer should carry such insurance anyway.  Tenant's insurance can cover the tenant's own possessions.

## 6. Conflict resolution

This section spells out what happens if a disagreement arises. The most straightforward and economical is for both parties to agree on a third party to facilitate conflict resolution.  If this fails, a more formal process involving a mediator might be necessary.

## 7. Signatures

When both parties sign the lease agreement, it becomes a legally binding contract. It is a good idea to have someone witness the signatures as an extra precaution. In addition, you can file a memorandum of lease with the town clerk's office to record the lease – attach to the title. .

**GO TO THE NEXT PAGE FOR YOUR SELF-TEST**

## Self test

Instructions: On a sheet of paper, write your answers to the following questions. Then check your answer to each question by clicking on the question below.

2. What is the minimum information to include in any lease?
3. Who is typically responsible for maintenance and repairs in a lease?
4. What are three examples of capital improvements?
5. What kind of insurance should a tenant carry?

## Resources

- Lease Agreement Guide for Landowners and Farmers
- Managing Landlord-Tenant Relationships: A Strategic Perspective
- Farm Rental Agreement Checklist
- Farmland Tenure and Leasing, from A Legal Guide to the Business of Farming, UVM Center for Sustainable Agriculture
- *Holding Ground: A Guide to Northeast Farmland Tenure and Stewardship*, Available for purchase at http://www.smallfarm.org/bookstore/
- *A New Lease on Farmland* available at www.smallisbeautiful.org
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- Sample Long-term Lease on Public Land
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**CLICK HERE FOR THE NEXT MODULE**

## Module 4

# Lease Negotiation and Management

In this module, you will learn about considerations when negotiating a lease and tips for maintaining good relations with farmland owners.

## Introduction

Once you have found that "perfect" piece of farmland, you will need to sit down with the owner and negotiate an agreement. Modules 1-3 of this tutorial will help you prepare for this meeting. In advance, spell out your "likes"—areas where you have some flexibility, and "needs"—absolutes for you to be able to farm that ground. For example, a "like" might be fencing (ideally already on the property, but you could install it yourself. A "need" might be access to a good, constant supply of potable water. You and the landowner will spend a good amount of time negotiating your and their "needs" to ensure that both parties are satisfied with an agreement.

## The Importance of Communication

The keys to any successful relationship, including between landowner and tenant, are trust and effective communication.

Lease agreements fail more often because there is a breakdown in communication than because of a breach or failure of one party or the other. If trust has not been established or is eroded over time or because of a specific disagreement, other problems are likely to build. It is really important to strive for clear, open and ongoing communication right from the beginning of the relationship.

Once an agreement is put into place, don't forget about the landowner. Keep the lines of communication open. You may feel too busy to bother (or bother with) the landowner but it pays off to keep in touch with him or her regularly. An annual meeting is the minimum good practice. A quick phone call, email or personal visit can help, especially if there is a change in the farmer's personal or business circumstances. An end of the season letter that reports how the season went is a nice way to keep in touch. All will help keep the landowner interested in the tenant's farm business and help build a fruitful long-term relationship.

## Determining Rental Rates

"What to charge" and "what to pay" rank among the top questions when negotiating a lease. There are number of ways to determine lease fees, depending on the type of lease chosen (see Module 2) and the financial goals of each party.

***Market rate***: A rental rate can be based on supply and demand – what the going rates are for comparable land in the area. If demand for farmland in the area is high, landowners often command higher rates. Typically cropland is higher than pasture and hay land. There is no one place or agency to find out about market rental rates, so you have to ask around.

***Landowner costs***: Landowners can calculate rent is by using the "DIRTI 5." These are the fixed costs associated with owning real estate -- Depreciation, Interest, Repairs, Taxes, and Insurance. Some non-farming landowners may actually charge a low –or no – rent in exchange for the property tax advantage they receive from having the property in active agriculture.

***Productive capacity:*** Rental rates may be calculated based on what the land is capable of producing. This is a function of soil type and condition, size and location of parcel, etc.

***Cost of production***: The farmer's actual costs can be used to guide a reasonable rental rate. It's important for the tenant to know what lease fee s/he can actually handle, and some landlords will want to be responsive to this reality.

***Social goals****:* Some landlords will accept a lower-than-market-rate rent because of personal or organizational goals.  For example, a land trust might want to lease its agricultural property at a low rate in exchange for specific habitat management.  An organization might offer affordable rates to a beginning farmer out on an interest in promoting new farmers in their area. .

**GO TO THE NEXT PAGE FOR YOUR SELF-TEST**

## Self test

*Instructions: On a sheet of paper, write your answers to the following questions. Then check your answer to each question by clicking on the question below.*

1. What is the difference between "likes" and "needs" in lease negotiation?
2. Why is communication with your landowner important?
3. What are three good ways to keep in touch with a landlord?
4. What are three ways to determine the rent?

## Resources

- Lease Agreement Guide for Landowners and Farmers
- Managing Landlord-Tenant Relationships: A Strategic Perspective
- Farm Rental Agreement Checklist
- Farmland Tenure and Leasing, from A Legal Guide to the Business of Farming, UVM Center for Sustainable Agriculture
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**CONGRATULATIONS! YOU'VE COMPLETED THE TUTORIAL!**

**GOOD LUCK WITH YOUR FARMING PURSUITS.**