Land Leasing

Introduction

Leasing additional land to increase production can be a useful option for growers. Leasing land can allow:

- improved cashflows
- increased scale and efficiency
- increased profit
- reduced debt risk
- growing the farming business without the need to purchase land.

Typically in agriculture, the tenant uses the land for an agreed time and fee. There are numerous variations on lease rates and types. Some include adjustments based on yields and market conditions. Normally the tenant carries the majority of the risk.

Landowners (Lessor) objectives

- financial return on the asset
- land and infrastructure maintained in good condition.

Landowners responsibility

The landowner is generally responsible for paying rates and rents, public liability insurance and infrastructure insurance.

Tenant's (Lessee) objectives

- Making a profit; generally by allowing increased scale and efficiency of production.
- Growing the farming business without buying land.

Tenant's responsibility

The tenant is responsible for operating costs and maintaining the land in a stable condition.

The tenant's objectives are generally focused on short-term profitability, whereas the landowner generally has objectives relating to the asset condition. This difference in objectives can be a point of conflict and must be recognized. This is the reason why longer-term leases are generally more useful to both parties.

The lease agreement

A written agreement should be constructed and include the following:

1. Land to be leased - Define the area and any parts excluded.
2. Identify other items included in the lease for use by the tenant.
3. Duration of the lease – lease term, options for renewal, penalties for early termination.
4. Premature discontinuation by the landowner or tenant (penalty arrangements so that both parties know the costs of late departure, early termination and can make plans accordingly).
5. Lease commencement – have an agreed starting date for the lease.
6. Lease payment – establish the amount and when it is to be paid.
7. Repairs and maintenance of pastures, equipment and structures - generally, all facilities are to be "maintained in present condition". It is recommended that the tenant and landowner make a joint inspection of all facilities, make notes and take photographic records.

Key Messages

Leasing can be a useful way to profitably expand a farming and vegetable business without the requirement for capital or the risk of debt.

This information sheet provides an overview of landowner and tenant responsibilities, highlights the importance of establishing a written lease agreement and provides guidance on determining lease rates.

Some leases also include soil tests for nutrients to ensure that 'nutrient mining' by the tenant does not occur over time.

8. Cropping paddocks (cash or fodder crops) - the agreement should specify the intensity of cropping; for example, the percentage of the property or area (hectares) that can be cropped in any year, if applicable.
9. Access to water - for irrigated crops is just as important as the land. Therefore access and reliability of water resources (the water and any irrigation facilities) must be agreed.
10. Capital improvements - generally tenants do not make capital improvements.
11. Conflict resolution - have a conflict resolution procedure defined in the lease document. Either nominate a single arbiter that both tenant and landowner accept, or nominate one each and an umpire.

How much is the lease worth?

There are several methods to determine what a lease is worth.

- Percentage of capital value.
- Percentage of the gross margin.
- Percentage of expected gross income.
- Market values. It is appropriate to seek a market value assessment from a rural real estate agent as a check.

Each business can afford a different lease rate, this depends on the production systems and profitability of crop types. Simply because the market rate is a certain amount per acre or hectare does not mean that all businesses can afford that amount.

It is critical that growers conduct their own marginal analysis on crop types and profitability of production to determine what rate can be paid for as a lease payment. There is no point leasing additional land if it is not profitable!

In many regions of Australia, lease land typically achieves 4-5% of the capital value of land. If a grower had to purchase this land from the bank the interest would be in the vicinity of 9-10%, plus rates. The difference between the two percentages is then available to the grower as increased profit.

Useful resources

Successful Land Leasing in Australia – A guide for farmers and their advisers- Second Edition by Rod Ashby and Duncan Ashby. RIRDC Publication No. 11/052. This publication can be downloaded from RIRDC – https://rirdc.infoservices.com.au/downloads/11-052

Summary

Leasing can be a useful way to profitably expand a farming and vegetable business without the requirement for capital or the risk of debt.

Disputes between tenants and landowners occur regularly. It is critical for parties to thoroughly discuss any agreement and to document the lease arrangement.

Document the condition of structures and land at the start of the lease; make notes, take photos or a video record to provide evidence. A written agreement is essential.

Ensure that the lease price for the land will be profitable for your production system, which may not necessarily be the market rate.

Tools and further resources

Further resources available that may be useful to consider business structures include:

- Increasing Productivity - Achieving economies of scale in vegetable production
- Scale of Vegetable Production - Profit calculator
- Collective Marketing - Selling vegetables profitably!
- A New Business Structure - The options and benefits
- Collaborative Business Models
- Legal Business Structures

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