



MANAGEMENT NEWS

CRP Sign Up Announced

Conservation Reserve Program (CRP) Sign-up 26 will be from May 5 to May 30, 2003 at your local FSA office. The USDA Farm Service Agency's CRP is a voluntary program available to agricultural producers to help them safeguard environmentally sensitive land. Producers enrolled in CRP plant long-term, resource-conserving covers to improve the quality of water, control soil erosion, and enhance wildlife habitat. FSA provides participants with rental payments and cost-share assistance. Contract duration is between 10 and 15 years. To be eligible for placement in CRP, land must be either :

- Cropland that is planted or considered planted to an agricultural commodity 4 of the previous 6 crop years from 1996 – 2001, and which is physically and legally capable of being planted in a normal manner to an agricultural commodity; or
- Certain marginal pastureland that is enrolled in the Water Bank Program;

Also eligible is land in a conserving use that has been sown down into an introduced grass. Hayed or grazed land (pasture) most likely will fit this criteria.

For more information on CRP, contact your local FSA office. Fact sheets and additional information can be found online at www.fsa.usda.gov. If you need assistance in deciding whether to offer your land in the CRP program, please give me a call or contact your local University of Tennessee Agricultural Extension Service office.

Equitable Crop Rent

(Adapted from PB1597, *Cropland Leasing Considerations*)

With passage of the 2002 Farm Bill, many landowners and producers have been evaluating their crop and cash lease arrangements. The two parties involved must select the type lease, which is best suited to their situation. Several considerations should be weighed carefully before the final selection is made. Both landowner and producer must determine what contributions of labor, capital and management skill they are able and willing to provide. They must also decide what production and price risks each party will bear. Making these determinations will give a general indication of the type of agreement which best fits.

The determination of an appropriate crop-share or cash lease arrangement will have a significant influence on net farm income and satisfaction of the two parties. The most effective lease will be structured to reward both parties in proportion to the value of contributions provided. Five important principles to follow in a crop-share lease agreement are:

- 1) Variable expenses that are yield increasing should be shared in the same percentage as the crop share. Fertilizer and lime are the most common inputs shared, although recently boll weevil eradication fees have also been shared.
- 2) As new technologies are adopted, share arrangements need to be adjusted to reflect their

- impact on costs and returns.
- 3) Both parties should share in total returns in the same proportion as they contribute resources. This principle implies that if a landowner contributed 25 percent of total resources and the tenant 75 percent, then a sharing of the crop 25/75 would be equitable. All inputs should be valued, including management and risk. A major problem with crop share leasing is that crop share percentages are influenced strongly by customary arrangements in the area. A further problem is that customary share arrangements change little over time, even though the relative values of land, machinery, labor and management may change markedly. A good example is cotton where production expenses have increased for the tenant and the crop share lease is the same as it was 20 years ago. The landowner and tenant should determine their contributions according to the actual operation, rather than on the basis of what has been, or is, customary for the area.
 - 4) Tenants and/or landowners should be compensated at the termination of the lease for the unexhausted portion of long-term investments. For example, lime applied to cropland usually lasts several years. If the tenant pays for the lime, then the lease should provide for a method of calculating the payment to the tenant for the unused portion of the lime if the lease is terminated before the total value of the lime is recovered.
 - 5) Communication must be maintained between landowner and tenant. If the lease does not follow the first four leasing principles, the farming operation may not produce at maximum economic efficiency, or one party may gain at the expense of the other. However, strict adherence to these first four principles cannot guarantee success, particularly if adequate management and effective communication between landowner and tenant are not used.

Developing a Fair Crop-Share Lease Arrangement

In publication PB1597 *Cropland Leasing Considerations* there is a worksheet and procedure to assist landowners and tenants in determining what is a fair and equitable crop-share lease. The worksheet is used to analyze a leasing situation in either of two ways:

- 1) Contributions approach. The percentage contribution of non-shared expenses of each party is determined. Then, the parties share other operating expenses and crops in the same percentage.
- 2) Desired-share approach. In this case, the parties specify a given percentage share basis (say 1/3 – 2/3), and then adjust contributions to fit this percentage.

If I can assist you in determining a fair crop-share lease, please contact me at (731) 635 – 9551.

Establishing a Fair Fixed-Cash Rental Rate

The cash lease has been a popular lease for many years. The primary attraction of this method to landowners is the minimal responsibility which must be assumed. This type of lease also provides tenants maximum operating freedom. If the decision is made to use a cash rental arrangement, what is a fair cash rent for the cropland? Four methods can be used to establish a fixed cash rent rate. These include an evaluation of:

- 1) Prevailing cash rental rates. General knowledge of cash rents in the area is needed with adjustments made for differences in land productivity.
- 2) Ability of Tenant to Pay. Many times tenants will pay too much for the use of land in their desire to control more land and spread fixed machinery costs over a larger acreage. Before bidding for land, tenants should carefully estimate how much capital will be available to pay for land use after deducting appropriate out-of-pocket costs, fixed costs on machinery and a return to management from expected gross revenue. Some farmers prefer to include only variable costs in estimating the maximum amount that can be paid. Their reasoning is that for a particular year, true fixed or overhead costs continue

regardless of whether or not the machinery and equipment are used. However, farm machinery will not be eventually replaced unless all costs are expected to be recovered. Tenants should estimate the maximum that can be paid and still allow all specified costs to be covered. The tenant should expect to lease land at something less than the maximum to allow a profit and remain sustainable.

- 3) Landowner's Cost. The landowner needs to calculate his or her cost of ownership. The major considerations in determining the owner's cost are land valuation and selection of an appropriate interest rate to apply to the land value. The per-acre land price should reflect a realistic market value for the cropland. A realistic interest rate is the 4 to 6 percent range, based on studies which show current cropland earnings to be in this range when land appreciation is excluded.
- 4) Landowner's Adjusted Net Share Rent. This approach determines the amount of rent the landowner would receive under a crop-share arrangement after paying any costs and after adjusting for reduced risk. Fixed cash rents are normally expected to be lower than share rents, since the landowner shifts yield and price risks to the tenant. Once the net share rent has been estimated, the parties must decide how much this rent should be adjusted for risk reduction to the landowner. In many situations, net share is reduced 10 to 20 percent to a cash equivalent, reflecting the reduced risk to the landowner. For example, if the landowner's returns based on the contributions approach and a $\frac{1}{4}$ - $\frac{3}{4}$ share agreement is \$100, discounting the share rent by 15 percent results in a cash equivalent of about \$85 per acre.

Compare the cash rent using the four approaches. The bargaining position of the two parties is important in establishing the specific cash rent. The bargaining process should provide an opportunity for each party to understand the position of the other. The most effective bargaining occurs when each party knows the value of his or her own contributions, the value of the other party's contributions and local leasing arrangements. Improved cash leases can lead to higher farm income, reduced soil and water loss in many cases, and more enduring personal relationships. These improvements can result from the use of farm economic principles which are designed to promote increased crop income and an equitable division of this higher income.

Opportunities for increased farm income and more satisfactory relationships provides incentive to improve farm lease arrangements. If equity considerations are important, the contribution approach to lease development should be studied. Breaking the bonds of tradition is not always easy, but is justified in many instances. Modern agriculture demands the use of up-to-date production methods and farm leasing principles.

For more information on cropland leasing, contact my office or your local University of Tennessee Agricultural Extension Service office and ask for PB1597 *Cropland Leasing Considerations*. For a copy of a written lease, contact my office at 731-635-9551 for Form 699 *Farm Lease Agreement*.

Crop Disaster Program Sign-Up Begins June 6, 2003

Sign-up for the crop disaster program, which will reimburse producers for qualifying crop losses in either 2001 or 2002, will begin June 6, with payments to begin shortly thereafter. Crop disaster payments must be calculated using the same formula used for the 2000 crop year. This means crop losses for 2001 and 2002 will be valued using the price election for Actual Production History (APH) crop insurance policies, or if that price is not available, a 5-year average.

Crop disaster payments are also subject to a formula which states that the sum of (1) the value of the crop not lost, (2) the disaster payment, and (3) the crop-insurance indemnity cannot exceed 95 percent of what the crop's value would have been, if there had been no loss. Crop disaster payments will be

reduced if the 95 percent limitation is exceeded. The value of the crop not lost and the 95 percent limitation will be valued at either the APH price election or the NASS season-average price, whichever is higher. A producer is eligible to receive a disaster payment when the producer's crop production is reduced by more than 35 percent from the expected yield. The expected yield is defined as the higher of: (1) the producer's APH yield; or (2) a county average yield.

For more information on Crop Disaster Program sign-up and the information you will need, contact your local Farm Service Agency.

May 20 GRP Listening Session in Dyersburg

The Risk Management Agency, USDA seeks to evaluate the Group Risk Plan (GRP) crop insurance to make determinations regarding possible program improvements. In order to complete the evaluation, one set of data needs to come from a series of listening sessions conducted face to face with producers and other stakeholders in order to obtain their feedback on how well the program is addressing their needs. Scientific Applications International Corp. (SAIC) will hold a RMA –approved listening session in Dyersburg on May 20 at the Lannom Center. The morning session beginning at 9:00 a.m. is for farmers with an afternoon session at 2:00 p.m. for insurance providers, agents, and other stakeholders.

The Group Risk Plan (GRP) crop insurance is designed as a risk management tool to insure against widespread loss of production of the insured crop in the county. GRP is a departure from traditional approaches to crop insurance protection, with less paperwork and generally less cost the Multiple Peril Crop Insurance (MPCI). The policy was developed on the basis that when an entire county's crop yield is low, most farmers in that county will also have low yields.

In West Tennessee, 17% of the acres in 2002 with crop insurance were GRP. Indemnity payments of \$12.5 million were paid for crop years 2001 and 2002 combined in GRP. If you have questions, concerns, or want to know more about GRP and/or crop insurance, I encourage you to attend this listening session on May 20.

If we can assist you in making farm financial planning or marketing decisions, please contact your local county Extension office or call the toll - free MANAGEMENT Information line at 1-800-345-0561 or myself at 731-635-9551.

Sincerely,



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COOPERATIVE EXTENSION WORK IN AGRICULTURE AND HOME ECONOMICS
The University of Tennessee Institute of Agriculture, U.S. Department of Agriculture,
and county governments cooperating in furtherance of Acts of May 8 and June 30, 1914.
Agricultural Extension Service
Charles Norman, Dean