
Pasture Leases

Quick Notes...

A lease is an agreement giving use of an asset to a lessee for a specific period of time at a specified rate without transfer of ownership.

Pasture leases may be calculated on a per head, per acre, or share of gains basis.

The terms of a lease agreement should be in writing.

Types of land rental agreements vary widely in each locality and from one livestock producing area to another. Most often these are based on long-standing traditions.

The purpose of this publication is to help landowners and livestock owners make informed decisions and to develop "fair" pasture lease arrangements. A sample pasture lease agreement can be found as a supplement to this document.

Although beef cattle examples are used in this publication, the principles and worksheets apply to all roughage-consuming livestock. Also, the values used in the various worksheets represent illustrations of the principles.

Landowners and livestock owners should use their own costs and prices to determine an equitable lease.

What is a Pasture Lease Agreement?

A lease is basically an agreement giving use of an asset to a lessee for a specific period of time at a specified rate. A lease does not transfer title of ownership nor an equity interest in the asset.

A pasture lease is an agreement in which the owner of pasture land receives a rental fee from the owner of livestock. The livestock owner uses the pasture and makes general management decisions as if owner of the land.

Labeling a document as a lease does not necessarily mean it is a lease according to the Internal Revenue Service (IRS). Questions concerning IRS treatment of a lease should be addressed by a tax management professional. Also, the legalities of the lease should be addressed by professional legal counsel.

Establishing Lease Rates: Per Acre or Per Head

The livestock owner can pay the landowner a rent based on acres of pasture or number of animals grazing the pasture.

The landowner's cost and livestock owner's return are two commonly used methods to determine a fair pasture rent per acre or head.

Landowner's Cost Method

For the landowner's cost method, the objective is to establish fair values for the resources and annual use charges.

Land: The value of land should be its fair market value for agricultural purposes. The influence of location near cities and other non-agricultural influences on value should be ignored.

Return on land investment: A percentage of land value indicates the landowner's return to the current value and also reflects pasture productivity. A percentage rate of 5 to 7 percent is suggested because (1) the current value of the land is used rather than the purchased price; (2) if the pasture were sold, the net dollars available to the seller would be lower than the current value due to income taxes and sale expenses; and (3) actual returns to land have been in the 3 to 5 percent range as an annual return above all charges, except land.

Real estate taxes: The actual real estate taxes due annually.

Land improvements: The average dollars spent annually for land improvements, conservation practices, and maintenance.

Building facility investment: A fair market value should be placed on fences, wells, ponds, buildings, and handling facilities. Ownership costs on this investment include depreciation, interest, repairs, taxes, and insurance.

1. *Depreciation:* Depreciable life for buildings and facilities usually ranges from 15 to 25 years.
2. *Interest:* The current interest cost on the average investment value (one-half the total value) should be used.

3. *Repairs, taxes, and insurance:* Facility repairs usually vary from 1 to 3 percent of the investment value. The charge for both taxes and insurance is about ½ to 1 percent.

Other costs: The average dollars spent annually for fertilizer, maintaining the forage resource, and any other costs.

Worksheet 1 illustrates ownership costs for 160 acres of pasture. The per acre ownership cost of \$19.94 establishes an asking lease price for one acre of pasture land. Rent per head is calculated by multiplying the \$19.94 by the carrying capacity of the pasture for the type and size of animal being considered. For example, a 625 pound beef animal may require four acres, which would result in \$79.76 per head per season (4 acres x \$19.94 per acre).

Livestock Owner's Return Method

For the livestock owner's return method, an enterprise budget is needed to determine how much the livestock owner can afford to pay for pasture rent. Enterprise budgets can be obtained from a Cooperative Extension office if livestock costs and returns are not known. Worksheet 2 illustrates the livestock owner's method.

The actual lease rate will probably be a negotiated value somewhere between the landowner's and livestock owner's figures.

Establishing Lease Rates: Share of Gains

The landowner and livestock owner may be interested in a share arrangement where the risk and probability of additional profit (or loss) is divided between the owners.

In such a case, risk can be effectively shifted by basing rent on a fixed amount per pound of gain. To illustrate this type of lease arrangement,

assume pasture rent for a yearling steer is \$9.00 per month. Total lease charges for a 6-month grazing season would be \$54 (\$9/month x 6 months). If a 270-pound gain would be a reasonable expectation, pasture rent would be \$0.20 per pound of gain ($\$54 \div 270 \text{ lbs.}$).

If the total weight gain turned out better than expected, say 360 pounds, the landowner would receive \$72 instead of \$54. However, if the animals gained only 180 pounds, the landowner would receive only \$36.00.

Establishing Rates: Other Factors

While each of the previously discussed methods may be used to establish pasture rental rates, there are other factors that influence the actual rental rate.

Market Rate: Market rate is the going price established by the bargaining of landowners and livestock owners. Estimated livestock inventories, market prices, and weather conditions are needed to estimate and negotiate the coming year's rental rates.

Location, Water, and Landowner Services: The value of water, location, and landowner services are subjective. However, these items have some value to the livestock owner.

Pasture location is important if the livestock owner is taking care of the livestock. The cost can be computed by estimating the number of trips per season times the number of miles times cost per mile. The number of trips should consider checking the cattle for health, minerals, and water supply as well as hauling or driving the cattle to and from the pasture.

Good quality water in proper locations improves gain. If water supplies go dry in mid-season, provisions must be made for hauling water or removing the animals. Who pays for these types of considerations must be spelled out in the lease agreement.

Landowner services vary from only collecting the rent to taking complete care of the livestock during the pasture season. A common method of charging for these types of services is a percentage of the gross rent.

Other factors: Rental rates per acre should reflect pasture productivity. Past stocking rates, weed growth, moisture, etc., all affect pasture productivity (stocking rates or carrying capacity). Pastures with low productivity rent for less than highly productive pastures.

Conflicts may arise if the livestock owner wants to stock the pasture with the maximum number of head per acre, and the landowner desires a low stocking rate as the rent is a fixed rate per acre. Continuous heavy stocking rates lower the quality of pasture by reducing the stand of grass and allowing weed growth.

Pasture rented on a per-head basis establishes a rate which may not adequately recognize differences in stocking rates. The livestock owner desires low stocking rates (higher gain per head) while the landowner desires higher stocking rates to increase income. Stocking rates and cattle weight may be the most important points for both parties to agree upon and enumerate in the lease.

Whole tract rentals are often part of a farm containing pasture. The rental rate for whole tracts is established by (1) the rate per head times the number of head allowed per tract or (2) the per acre rate times the number of acres in pasture.

Putting the Agreement in Writing

It is highly desirable to put the terms of a lease agreement in writing. A written lease agreement enhances understanding and communication between all involved parties, serves as a reminder of the terms originally agreed upon and provides a valuable guide for

the heirs if either the landowner or tenant dies.

Every lease agreement should include certain items--the names of the parties involved, an accurate description of the property being rented, the beginning and ending dates of the agreement, the amount of rent being paid and the signatures of the parties involved.

Furthermore, other provisions (such as the rights and responsibilities of both parties) which provide for most of the concerns of both the landowner and tenant should be included in every lease.

*Notes...
Network*

*(For More Information) Contact: Jeff Tranel, Ag & Business Management, CSU
Extension (719) 549-2049, Jeffrey.Tranel@colostate.edu
(Updated August 2008)*

WORKSHEET 1. LANDLORD OWNERSHIP COSTS PER ACRE AND HEAD

A. Land Investment:

Interest	\$ <u>36,000</u>	land value x <u>6</u> %	\$ <u>2,160.00</u>
Land taxes	\$ <u>36,000</u>	land value x <u>1</u> %	\$ <u>360.00</u>
Land maintenance	\$ _____	land value x _____ %	\$ _____

B. Other Investments:

Fences	\$ <u>4,000</u>		
Corrals	\$ <u>1,000</u>		
_____	\$ _____		
Total			\$ <u>5,000.00</u>

Depreciation	\$ <u>5,000</u> ÷ <u>20</u> years		\$ <u>250.00</u>
Interest*	\$ <u>5,000</u> ÷ <u>6</u> %		\$ <u>300.00</u>
Repairs	\$ <u>5,000</u> ÷ <u>2</u> %		\$ <u>100.00</u>
Taxes			\$ <u>10.00</u>
Insurance			\$ <u>100.00</u>

C. Other Costs:

Fertilizer		\$ _____
Other		\$ _____

D. TOTAL OWNERSHIP COSTS \$ 3,190.00

E. Number of Pasture Acres: 160 acres

F. Ownership Costs/Acre: \$ 3,190 total costs ÷ 160 acres \$ 19.94

G. Stocking Rate: 4 acres per head

H. Ownership Costs/Head/Season: \$ 19.94 costs/head x 4 acres/head \$ 79.76

*A percentage rate of 6% on \$5,000 is equal to 12% of the average investment of \$2,500.

WORKSHEET 1. LANDLORD OWNERSHIP COSTS PER ACRE AND HEAD

A. Land Investment:

Interest	\$ _____	land value x _____ %	\$ _____
Land taxes	\$ _____	land value x _____ %	\$ _____
Land maintenance	\$ _____	land value x _____ %	\$ _____

B. Other Investments:

Fences	\$ _____		
Corrals	\$ _____		
_____	\$ _____		
Total			\$ _____

Depreciation	\$ _____ ÷ _____ years		\$ _____
Interest*	\$ _____ ÷ _____ %		\$ _____
Repairs	\$ _____ ÷ _____ %		\$ _____
Taxes			\$ _____
Insurance			\$ _____

C. Other Costs:

Fertilizer			\$ _____
Other			\$ _____

D. TOTAL OWNERSHIP COSTS

\$ _____

E. Number of Pasture Acres: _____ acres

F. Ownership Costs/Acre: \$ _____ total costs ÷ _____ acres \$ _____

G. Stocking Rate: _____ acres per head

H. Ownership Costs/Head/Season: \$ _____ costs/head x _____ acres/head \$ _____

*A percentage rate of 6% on \$5,000 is equal to 12% of the average investment of \$2,500.

