Lease Supplement for Investing in Improvements on a Rented Farm

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File C2-07

The purpose of this lease supplement is to encourage cooperation between tenants and landowners who wish to obtain needed improvements, facilities, and buildings on a rented farm. Often rented farms are in need of additional buildings, facilities, major repairs, or soil improvements. Many of the additions and improvements that are needed on a rented farm will not be made unless the tenant pays for part or all of the cost. But tenants are not likely to make important contributions toward farm improvements unless they are sure of repayment for any unexhausted value of their investments in case they have to discontinue farming the property.

Procedure

First step: Agree on the improvements to be made: what each party will furnish, rate of depreciation, and estimated value of tenant's investment in each major improvement or addition.

Second step: Record and sign the agreements on the lease supplement. Fill out one copy each for landowner and tenant.

Suggested Rates of Depreciation

The initial cost of each improvement should be depreciated over a reasonable length of time. Straight-line depreciation is suggested because it is simple and it is commonly used for accounting purposes. For major improvements such as a livestock building, machine shed, or livestock production facility, a depreciation period of 15 to 25 years is suggested. For minor improvements such as fences or corrals, a shorter depreciation period may be used. However, the two parties may use any rate of depreciation they can agree upon. Farm income tax depreciation schedules are not particularly useful, though, because they often allow assets to be depreciated more rapidly than their actual market value decreases.

Spreading Limestone

The rate of depreciation and value of limestone varies with the type of soil, cropping system, the amount of limestone applied, and other factors. Under average conditions, the value of limestone may be assumed to last three to five years.

Commercial Fertilizers

The residual value beyond the year of application of fertilizers depends on a number of factors, including nutrients applied, rate of application, soil, crops to which applied, and seasonal weather conditions. The level of these nutrients in the soil at the time of the fertilizer application should also be considered. On farms where the rate is designed to maintain the present level of fertility, no allowance is usually made for fertilizer residual. On farms where the fertility level is low and the application rates are high relative to anticipated annual use, it may be desirable to specify a carry-over value of fertilizers.

Farm Structures and Repairs

A tenant on a cash or crop-share lease sometimes wants special improvements beyond what the landowner will furnish for machinery storage, grain storage, or livestock production. The landowner may receive little, if any, direct return from such an investment. If the landowner will not provide such a structure, then the tenant may offer to make the improvement provided the landowner will guarantee payment for any unused value in case the tenant moves on before fully realizing the value of the investment. If the structure fits in with the landowner's improvement plan, the landowner may provide a portion of the investment and safeguard the tenant for a period of years on the part the tenant provides.

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Farm Drainage and Terraces

Farm drainage and terraces usually are the entire responsibility of the landowner. If the tenant bears all or part of the expense of tiling or ditching for drainage or constructing terraces, a suitable depreciation period for the tenant's investment should be used. In some cases, the tenant may provide labor and/or machinery for making such improvements. Ag Decision Maker File A3-10, Iowa Farm Custom Rate Survey, https://go.iastate.edu/AGDMA310, can be used to value the tenant's contribution in such a case. More information about tiling can be found in AgDM Information File C2-90, Understanding the Economics of Tile Drainage, https://go.iastate.edu/AGDMC290.

Additional resources related to leasing in Iowa may be found on the <u>Ag Decision</u> <u>Maker Leasing website</u>, https://go.iastate.edu/AGDMLEASING.

Table 1. Suggested depreciation rates.

	Years	Annual Rate
Livestock production facilities	10-20	5-10%
Machinery storage, grain bins	15-20	5-7%
Tile lines	10-15	7-10%
Terraces	10-15	7-10%
Fences	15-20	5-7%
Lime	3-5	20-33%

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Description of Farm: County Acres Township Section(s) Acres	Description of Farm : County	Township	Section(s)	Acres	
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- 1. In consideration of the agreements herein contained, the signers agree that the improvements listed in column A (below) have been completed on the above-described farm.
- 2. It is agreed that the signers will share contributions and costs necessary to the completion of these improvements as set forth in column B.
- 3. It is agreed that the estimated value or cost of the tenant's contributions will be listed in column C.
- 4. It is further agreed that the estimated value or cost of the tenant's contributions will be depreciated at the uniform annual rate listed in column E. The year of first depreciation is to be listed in column F.
- 5. If for any reason the tenant leaves the farm before the tenant's estimated value or cost (column C) is fully recovered through annual use and deprecation (column E), then the landowner will pay the tenant for the remaining undepreciated value of the tenant's investment (column K).
- 6. It is agreed that each item as set forth opposite the signatures of the landowner and tenant will be viewed as a separate contract supplemental to the lease. New items may be agreed upon at any time during the term of the lease and recorded in the table below.

	B. Cost of contributions by landowner (L) or by tenant (T)					C. Total cost of tenant's	D. Years over which	
A. Type and location of improvement	Mate Landowner	erials Tenant	Machin Landowner	ne work Tenant	Landowner	bor Tenant	contribution (total from column B)	improvement will be depreciated
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		H. Sig	Use to calculate remainder after lease has ended.				
		I hereby accept my indicated s improvements recorded in co	I. Year	J. Total	K. Remaining value to be		
	G. Date signed	Landowner	Tenant	lease ends	cost to deduct E × (I – F + 1)	repaid to tenant (C – J)	