
Lease Supplement for Investing in Improvements on a Rented Farm

Ag Decision Maker

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

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the improvement provided the landowner will guarantee payment for any unused value in case the tenant has to move before fully realizing the value of the investment. If it is a structure that 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.

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. The Iowa Farm Custom Rate Survey (AgDM File A3-10) 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*.

Suggestion	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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