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8-14-2019

# Accounting for Risk: Agricultural Land Leases and Natural Disasters

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Jansen, Jim and Stokes, Jeff, "Accounting for Risk: Agricultural Land Leases and Natural Disasters" (2019). *Cornhusker Economics*. 1015.

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# Cornhusker Economics

## Accounting for Risk: Agricultural Land Leases and Natural Disasters

Market Report	Year Ago	4 Wks Ago	8-10-19
<b>Livestock and Products,</b>			
<b>Weekly Average</b>			
Nebraska Slaughter Steers, 35-65% Choice, Live Weight. . . . .	*	*	*
Nebraska Feeder Steers, Med. & Large Frame, 550-600 lb. . . . .	177.62	183.32	173.82
Nebraska Feeder Steers, Med. & Large Frame 750-800 lb. . . . .	162.42	16156	156.48
Choice Boxed Beef, 600-750 lb. Carcass. . . . .	205.91	214.64	216.04
Western Corn Belt Base Hog Price Carcass, Negotiated . . . . .	43.68	*	*
Pork Carcass Cutout, 185 lb. Carcass 51-52% Lean. . . . .	70.35	7114	87.97
Slaughter Lambs, woolled and shorn, 135-165 lb. National. . . . .	160.18	166.65	159.96
National Carcass Lamb Cutout FOB. . . . .	370.67	394.50	395.17
<b>Crops,</b>			
<b>Daily Spot Prices</b>			
Wheat, No. 1, H.W. Imperial, bu. . . . .	4.91	4.09	3.45
Corn, No. 2, Yellow Columbus, bu. . . . .	3.40	4.42	3.87
Soybeans, No. 1, Yellow Columbus, bu. . . . .	768	8.16	7.77
Grain Sorghum, No.2, Yellow Dorchester, cwt. . . . .	5.29	680	5.98
Oats, No. 2, Heavy Minneapolis, Mn, bu. . . . .	2.91	3.76	3.01
<b>Feed</b>			
Alfalfa, Large Square Bales, Good to Premium, RFV 160-185 Northeast Nebraska, ton. . . . .	*	172.75	*
Alfalfa, Large Rounds, Good Platte Valley, ton. . . . .	102.50	*	115.00
Grass Hay, Large Rounds, Good Nebraska, ton. . . . .	150.00	100.00	100.00
Dried Distillers Grains, 10% Moisture Nebraska Average. . . . .	122.50	149.50	136.50
Wet Distillers Grains, 65-70% Moisture Nebraska Average. . . . .	40.00	44.50	40.50
<b>* No Market</b>			

According to recent findings from the USDA Agricultural and Resource Management Survey, agricultural land rent totaled \$2.44 billion in Nebraska for 2018. The survey found rent as the third largest farm and ranch production expense (USDA-NASS 2019). Natural disasters limiting the ability of farmers or ranchers to fully utilize rented land pose a financial risk to these operators.

The 2019 floods and related natural disasters have left many landlords and tenants across Nebraska wondering how resulting damages will influence their agricultural properties. Contractual lease arrangements may have not fully accounted for these natural disasters. This article provides guidance on evaluating damages, considerations for remediating land issues, and natural disaster lease provisions.

### Evaluating Damages

Natural disaster events on land may leave *minor* or *major* damages on agricultural property. Documenting these issues for federal, state, or local authorities remains critical to participate in various disaster recovery programs when available. Issues with each of these two broad types of disasters might include the following:

*Minor damages* may include various kinds of debris or foreign objects scattered across a field. There may also be minor erosion or washout issues. Use of common agricultural equipment and implements in addition to hand labor may be necessary to remedy minor damage.

*Major damages* may include major transformations to the land such as large washouts, extreme erosion, and large deposits of foreign materials such as soil or debris. These issues may limit farmers or ranchers from utilizing a portion or all of the property. Specialized heavy construction equipment may be necessary to correct major damage.

Landlords have the primary responsibility for correcting natural disaster damages on rented land and remediating the sites to suitable states for farming or ranching. Depending upon the landlord or tenant engaged in these lease arrangements, the limited ability of one party over the other may require hiring outside resources to correct the issues (Vyhnalek 2019).

### **Considerations for Remediating Land Issues**

The ultimate goal of remediating natural disaster issues on properties is restoring the land as close as possible to the condition prior to the major event. Depending upon the type of lease and the provisions, this will influence the rights and delegation of duties for each party.

#### *Lease Types*

Cash rent and crop share account for the majority of land lease arrangements across Nebraska. In cash leases, landlords receive a cash payment for use of crop or grazing land. Contractual language in the lease likely requires full payment for the use of the land unless other provisions specifically address the issue.

Under contract law, if an event renders the property unusable for the entire growing season, the tenant may have cause for vacating the premise and avoiding any lease payment obligations. Exercising this option may cause dire consequences between landlords and tenants. Tenants eligible for prevented planting with crop insurance might consider payment rates that at least allow landlords to cover property taxes for the land.

Producers operating on a crop share lease may not have to revise the provisions of the lease due to the inherent risk-sharing feature of the rental rate. As crop yield varies, the lease payment (crop yield) fluctuates in proportion to the yield. Prevented planting and disaster assistance payments pay landlords and tenants in proportion to their respective share of the yield if both parties purchase crop insurance or participate in a particular government program. Unders

tanding the terms of crop insurance as part of a crop share arrangement remains crucial for both parties involved in a lease and a key factor to visit about with crop insurance agents.

#### *Contributions of Tenants*

Many retired and absentee landowners may not have the ability or time to help correct damages on their rented property in the event of a major disaster. Tenants possessing the ability, time, or equipment might be able to fix minor issues on properties. Some tenants may even be able to correct major damages if they own very large or specialized equipment.

Accounting for these contributions remains important for lease arrangements. Prudent landowners may consider negotiating a discount on cash rent when the tenants provide use of their time, skills, or equipment in fixing a disaster issue. In cases where tenants may be willing and able to correct minor or major damages, adjusting the effective cash rental rates might be an equitable method for incentivizing the other parties to help correct these issues.

The terms and obligations of each party must be documented as part of the lease arrangement. Depending upon the disaster event, various forms of financial assistance may be available from the federal, state, or local government authorities to offset the expense of correcting issues.

### **Natural Disaster Lease Provisions**

Accounting for the unknown provides the greatest insurance policy for landlords and tenants engaged in an agricultural lease. Identifying the responsibilities, duties, and role of the parties involved in the lease ensures activities happen in a timely manner.

#### *Adjusting Rental Rates*

Setting equitable rental rates which account for the requirements of parties engaged in a land lease needs to be a priority when considering future adjustments. Landlords have fixed expenses such as property taxes. Tenants may pre-pay for inputs on cropland or need forages each year for grazing livestock. Disruptions to the annual production cycle for landlords and tenants create difficulties for each party.

Provisions in the lease may outline the methods for adjusting the rental rate when a disaster limits the

ability of a tenant to utilize a property. Provisions may also define compensation rates for tenants providing remediation services to a property. Certain minimum rental rates on cropland might be designed to cover fixed expenses, such as property taxes, and be offset by prevented planting payments when applicable. In any case, the adjusted rental rate seeks to minimize the financial burden on landlords and tenants.

#### *Documenting Disaster*

Documenting damages remains essential in understanding the extent of issues on the property resulting from natural disasters. Lease provisions can define the party responsible for documenting and communicating the damages to the other party or government agency. Tenants may be willing to provide this service if landlords are absentee or have limited ability to visit the land. Other terms to include in the lease might be the time frame in which the damages must be reported to the appropriate authority.

#### *Correcting Damages*

Designating the responsibilities of each party to correct minor and major damages in a lease develops a plan for dealing with these unforeseen events. In cases where tenants provide remediation services to correct land issues, specific lease provisions might include the timeline for carrying out the work and reimbursement rates.

#### *Amending the Lease*

Any changes made to the land lease to address disaster damages should be placed in writing and documented appropriately as an addendum to reduce any issues arising between landlords and tenants.

## **References**

- Vyhnalek, A. (2019, 28 March). Should Leases be Adjusted for Flood-Damaged Farm Ground? *Crop-Watch*, retrieved August 7, 2019 from University of Nebraska-Lincoln: <https://cropwatch.unl.edu/2019/flooded-cropland-lease-adjustments>.
- USDA-National Agricultural Statistics Service. (2019, August). Farm Production Expenditures 2018 Summary. *Farm Production Expenditures by Farms Reporting, Average per Farm, and Total – Nebraska: 2017 and 2018*, retrieved August 7, 2019 from United States Department of Agriculture Economic Research Service: <https://usda.library.cornell.edu/concern/publications/qz20ss48r>.

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