

Conservation Provisions in Leases

Various entities are encouraging farmers to adopt practices that promote soil conservation and ecosystem services. State and federal government agencies provide cost share for a host of conservation practices. In addition, various non-governmental conservation and land trust organizations have programs to encourage landowners to enhance and preserve habitat on their property. Emerging ecosystem markets pay farmers and landowners for practices such as carbon sequestration and improving wildlife habitat. Conservation practice can affect leases and the relationship between landowners and tenants.

This guide presents topics to address when incorporating conservation and ecosystem services into a lease agreement.

Characteristics of conservation and ecosystem services that impact leasing agreements include these:

1. the activities may interfere with other landowner objectives such as crop production, potentially reducing yields in one or more years,
2. the adoption costs are usually incurred at the beginning while benefits are realized several years later,
3. the time between initiating the conservation activity and observing benefit is uncertain, and
4. the benefits may be difficult to quantify.

Each of these characteristics impact the way a lease agreement might incorporate conservation activities.

Conservation practices such as tiling, terracing and planting grassed waterways may interfere with production in the year they are implemented. Over the long term they are expected to benefit yield and improve soil conditions, but first-year yield losses are a cost of adoption.

Conservation costs are incurred as the activity is done before any benefit is realized. Some conservation practices, such as no-till production and implementing the 4Rs of soil fertility might be expected to reduce the costs of production. Other conservation practices require labor, machinery, products, or some combination of these. The cost of each of these depends on several

factors. A custom operator needs to recover all the costs of performing an activity. A farmer (either tenant or landowner) with the available time and equipment may perform the same activity for less cost. But even the farmer's labor and equipment incur an opportunity cost.

Conservation practices

Permanent practices

- Grassed waterways
- Wetlands
- Riparian zones
- Terraces
- Ponds
- Pasture improvements
- Fencing
- Diversion ditches
- Establishing trees and shrubs

Temporary practices

- Conservation tillage
- Following contours
- Liming of soil
- Cover crops
- Crop residue preservation

Note: this list is not exhaustive. It provides a sample of conservation practices that might be included in a land lease.

Conservation is intended to maintain or improve the productivity of the land. Benefits may not be attained for several years after the conservation practice has been implemented. For example, cover crop studies indicate that it may take three to five years before production increases due to improved soil health. Reducing soil erosion extends the life of the soil resource, and this may result in receiving a higher price when the land is sold.

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Conservation benefits are uncertain, subject to factors outside the control of farmers. Adverse weather conditions might thwart the efficacy of some conservation practices. Some benefits, such as improved water infiltration, may occur in some years but not others. Even observable benefits are difficult to quantify because a monetary value cannot be assigned to how a ton of soil not entering a stream or an inch of water not running off the field affects production levels or land value.

Landowners, tenants, businesses and governments recognize the importance of conservation practices – despite the challenges. Some people accept costs of conservation for ethical reasons; others consider the costs to be long-term investments expected to provide a future return. A leasing relationship adds another consideration to the question of how to incorporate conservation and ecosystem services. The four steps discussed below provide guidance for modifying lease agreements.

Step 1. Understand objectives

A lease is simply an agreement between a property owner and a tenant. The property owner agrees to allow the tenant to use the land for specific purposes over a specified period. The tenant agrees to pay the landowner for the use of the land. Each party understanding the goals of the other is the first step in incorporating conservation provisions in leases.

Tenants usually rent farmland to benefit their business. They are interested in making an annual return by using their labor, management and physical assets in farming. Tenants are also interested in conservation. Research indicates that tenants tend to institute conservation practices on their owned land before they do on their rented land. The tenant may visualize a barrier to conservation that may or may not truly exist on leased land.

If a tenant initiates a conversation with a landowner about conservation, it is likely the tenant thinks the conservation activity will increase profitability. Tenants proposing conservation activities will more likely succeed if they understand the landowner's objectives in owning the land and make their proposal meet the landowner's objectives.

Landowners have varied reasons for owning land. Some landowners focus on cash flow, especially if they are dependent on land lease income for living expenses. Other landowners consider property ownership an investment – seeking property value appreciation over time. Strong emotional ties to the property may cause some landowners to want to preserve the land and make improvements. Still, other landowners have ethical perspectives that spur them to institute conservation

practices with few financial considerations. Often, a mix of these reasons work together in the landowner's decision making.

A landowner asking the tenant to incorporate a conservation practice into the lease is more likely to succeed if the tenant's objectives, resources and constraints are understood.

Step 2. Explore opportunities

Conservation opportunities are site-specific. No one activity is appropriate for every field. The right conservation activity or practice is a well-planned pursuit.

Conservation ideas may come from the landowner or tenant recognizing a problem that needs to be remedied, from an organization that is advertising services or from opportunities to participate in a market connected to specific farming practices. The conservation idea likely meets one or more of the objectives of the landowner and/or tenant.

Each objective can typically be accomplished through multiple methods. For example, an objective of reducing erosion may be easily reached by changing tillage practices. It may also require more extensive activities, such as terracing or installing grassed waterways. Discovering all the ways to accomplish a conservation objective opens opportunities to work within the resources and constraints of each party in the lease.

The U.S. Department of Agriculture Natural Resource Conservation Service (NRCS) provides technical assistance in deciding which activity is most suitable for a particular field and how to implement that activity. These NRCS conservation plans describe necessary activities and products and estimate costs to complete the plan. Conservation plan approval may lead to USDA financial assistance.

Non-governmental organizations also provide various types of technical assistance. Some provide financial resources for conservation practices. The [Missouri Land Trust Coalition](http://missourilandtrusts.org) (missourilandtrusts.org) provides links to many such organizations working in Missouri.

Research reports indicate that transaction costs are critical to successful changes in land management. Transaction costs include things such as education on what activities are appropriate for the land, investigation of what agencies and organizations can assist, obtaining a viable conservation plan, getting project estimates from companies able to fulfill the plan and employing an attorney to incorporate the practice into a lease agreement.

The party in a lease that desires a conservation change may need to incur most of the transaction costs and to reduce these costs to the other party.

Sources of information on conservation activities

Government

- USDA Natural Resources Conservation Service
- Local Soil and Water Conservation Districts

Non-governmental organizations

- Land Trust Alliance
- Missouri Land Trust Coalition
- American Farmland Trust
- The Nature Conservancy
- Quail Forever and Pheasants Forever
- National Fish and Wildlife Foundation

Markets

- Indigo
- Nori
- Soil and Water Outcomes Fund
- Ecosystem Service Market Consortium

Note: this list is not exhaustive. It provides a sample of entities that are engaged in conservation practices.

Economic considerations

Establishing a conservation practice often requires purchasing materials and services. Some landowners or tenants may have the ability to perform some of the services. But still, implementing a conservation practice requires paying for products like seed, pipes, fencing, fuel and labor.

An engineering/conservation plan may also be needed to ensure the activity accomplishes its intended purpose. NRCS field conservationists or Technical Service Providers (TSPs) contracted by NRCS may develop a working plan. After the plan is written, the landowner or tenant will decide whether to implement the plan. Not implementing an approved NRCS plan can cause NRCS to be hesitant to develop subsequent plans. This might mean that a tenant communicates with the landowner before requesting a plan to determine if the landowner is willing to consider a conservation practice.

The landowner almost always must sign off on an NRCS conservation plan. Permanent improvements require landowner permission to conduct the activity. Even short-term activities (e.g., no-till and fertility practices) have multi-year time frames. These require the landowner to agree to multi-year terms or the tenant to

show he or she has a lease of sufficient length to meet the requirements.

If any entity, such as the NRCS, a land trust, contractor, consultant, or an ecosystem market is going to be involved in the conservation practice, both the landowner and tenant need to understand how the entity involvement affects the lease. Is a long-term lease required? Does it require landowner approval? Who will get cost share dollars? Is the person receiving payments the one contracting to have an activity conducted on the land?

In addition to initial implementation costs, conservation practices typically have maintenance costs. These costs are usually cash outlays. Conservation practices may also result in less land in production and lower yields on affected land in the short run – especially if the conservation practice interferes with production in the year it is instituted.

Ideally, costs will be offset by increased yields or asset values over time. A plan should estimate the time needed to recoup the investment in the conservation activity and assess the likelihood of the outcomes and benefits. Strengthen the plan by documenting who did the plan estimates and the sources of data.

Step 3. Communicate

The party wanting a change in a lease is more likely to succeed when coming to the other with a clear, but flexible, plan that recognizes the other party's objectives and need for information.

Simply initiating a conversation about conservation practices may clarify the objectives of both parties and give insight into how to best move forward. Communication may involve the landowner pointing out what the tenant is doing on another field and asking their experience. The conversation can move towards discussing whether it would be appropriate for the leased field.

The party in a lease that has the strongest incentive to begin a particular conservation practice is likely the one who can best advance the idea to the other party. For example, a landowner wanting to reduce erosion can come to the tenant with several options and a preferred plan for reducing erosion. Alternatively, a tenant may recognize that certain portions of a farm are not profitable in many years. The tenant would explore alternatives to farming those areas and present to the landowner how the top one or two alternatives would affect the lease.

Some landowners are very familiar with their land and may have strong ideas and opinions of what conservation activities are most likely to succeed. Other landowners may have less familiarity with their land or

the range of conservation alternatives. These landowners may lean more on the experience of the tenant to provide proper information. Some tenants may be hesitant to suggest conservation practices if they are not familiar with the landowner's objectives in owning the land.

Communicating desired changes to leases is a time-intensive process that will likely require multiple discussions over a period of weeks or months. Once a general agreement is reached, time will be required to draw up a final plan and find resources to accomplish the plan. Bringing a proposal right before lease renewal may meet resistance merely because it will take more time to evaluate the proposal than is available.

Occasionally, landowner and tenant may reach an impasse if one party insists on a conservation activity and the other party refuses. If the disagreement is strong enough, one party may desire to end the lease. Ending a lease also takes time. Both parties must follow any written lease termination clause or state laws, in the case of a verbal agreement.

Communication also requires clarity. Negotiation is fostered by having a clear path forward focused on how the practice will be implemented. Asking and answering questions (see sidebar) and clearly outlining necessary steps for beginning new practices can help to communicate to the other party that a plan can work.

Step 4. Document agreement

Documenting the agreement might mean writing an entirely new lease agreement or adding an addendum to an existing agreement.

Because conservation activities span multiple years, it is important to document discussions and agreements about conservation activities in land lease agreements. Documentation clarifies what each party has agreed to and each party's roles and responsibilities. Documenting the agreements about how the conservation practice will be instituted assists in successfully implementing the plan.

Below are some considerations when including conservation provisions in leases.

Written leases, important to any rental agreement, are especially important when conservation provisions are included in a lease. Many conservation activities are multi-year activities. Writing them into the lease clarifies what was agreed upon and how to handle questions about conservation practices.

Multi-year leases can assure the tenant that his or her conservation investments can be recaptured. Offering multi-year leases might also enlarge the pool of tenants interested in land with conservation restrictions. Landowners may resist long-term leases due to factors such as unsatisfactory tenant performance, agreed upon

rental rates not changing as market rental rates do, or the lease making the property more difficult to sell. Flexibility in terms can be included in multi-year leases to address these issues.

Discussion topics for adding a conservation activity to a land lease

- What is the specific conservation need for this field?
- What are ways this need can be met?
- Who can draw up a conservation plan for this field?
- What products will need to be purchased?
- What activities will need to be performed?
- Who will conduct the necessary activities?
- Who will pay for products purchased?
- Who will pay for activities performed?
- When will the improvement begin? End?
- What maintenance will be required?
- When will maintenance be required?
- Who will maintain the improvements?
- What are the expected impacts of this activity in year 1? 2? 3?
- What cost share or market opportunities exist?
- What markets exist that impact this conservation activity?
- What governmental and non-governmental entities might help with this activity?
- What inspection and compliance activities will a funding entity require?
- Who will any help with ongoing inspection and compliance activities from funding entities?

Incorporating flexibility can give both landowners and tenants the necessary freedom to confidently enter into a lease agreement. Tenants may be most concerned with recouping investment in conservation activities on rented ground. Amortization schedules can provide ways that the tenant is repaid should the lease end before the conservation benefits are realized.

Landowners may be most concerned about exiting a lease if certain conditions—such as illness, death, or poor tenant performance—arise. Termination provisions can be incorporated into a multi-year lease.

Various rental payment plans can provide flexibility in rents over time to account for the impact of the conservation activity on production. Graduated rents,

flexible cash leases and crop share agreements all allow flexibility in rental payments.

Sharing risks and rewards from conservation activities helps create incentives to implement the practices. Risk sharing can be accomplished by using crop share or flexible cash lease arrangements. Short-term reduction in production (e.g., less land planted because of grassed or riparian zones) will impact the landowner as well as the tenant. Establishing rent on tilled acres, rather than total acres, can account for any acreage that is taken out of production for a conservation objective.

Cost sharing by the landowner may help the tenant incorporate the landowner’s desired conservation practice. The landowner and tenant would discuss both establishment and maintenance costs associated with conservation practices, determining each party’s responsibility for costs and the limits of each party’s liability.

Graduated rents may be used to discount rent for tenants who incorporate conservation practices. An example might be a 10% discount in rent in year 1, a 5% discount in years 2-5 and no discount after year 5. A landowner might offer this type of graduated rent for

planting cover crops which often begin to show increased yields 3-5 years after initiating the practice. The reduced rent recognizes the upfront costs of the planting cover crops that are expected to increase yields in the future. When conservation activities begin to pay back, the rent no longer needs to be discounted. Graduated rents, which are a form of sharing the cost of the conservation activity, need to be thoroughly discussed so each party understands what is happening and why.

Amortizing the cost of establishing conservation practices specifies how much will be repaid to the tenant if the lease ceases before the tenant’s contribution is fully depreciated. Conservation improvements on land (e.g., grassed waterways, fencing, terraces) may have a depreciable life. If the tenant contributed to the establishment costs of these assets, it may be wise to include in the lease. Information that needs to be recorded to calculate repayment due to the tenant for early lease termination is shown in Figure 1. Download the [Improvement Amortization Schedule for Leases \(XLSX\)](https://extension.missouri.edu/media/wysiwyg/Extensiondata/Pro/AgBusinessPolicyExtension/Docs/improvement-amortization.xlsx) (extension.missouri.edu/media/wysiwyg/Extensiondata/Pro/AgBusinessPolicyExtension/Docs/improvement-amortization.xlsx) to use as a template.

Description	Example	Improvement 1	Improvement 2	Improvement 3	Improvement 4
Improvement (description and location)	Fencing				
Date completed	8/1/2020				
Contribution of tenant to improvement	\$10,000				
Years over which improvement will be amortized	20				
Annual amortization	\$500				
Date amortization begins	8/1/2020				
Date lease ends	12/31/2025				
Years of amortization	5.4				
Amortized value	\$2,709.59				
Amount to repay tenant	\$7,290.41				

Figure 1. Record this information to calculate repayment due to tenant for early lease termination.



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