UNITED STATES DEPARTMENT OF AGRICULTURE
Farm Service Agency
Washington, DC 20250

Notice DCP-172

For: State and County Offices

Impact of Various Lease Agreements on DCP Participation

Approved by: Deputy Administrator, Farm Programs

1 Overview

A Background

The Farm Security and Rural Investment Act of 2002 (2002 Farm Bill) mandates that the Secretary shall provide:

- adequate safeguards to protect the interests of tenants and sharecroppers
- for sharing direct and counter-cyclical payments among the producers on a farm on a fair and equitable basis.

7 CFR § 1412.504 regulations outline provisions about sharing DCP payments, including the conditions upon which a lease shall be considered a cash or share lease.

Recently a number of requests have been received for clarification about:

- flexible or variable leases and whether these agreements should be considered cash or share leases for DCP purposes
- the impact to CCC-509 payment shares for bonuses paid to landowners.

B Purpose

This notice:

- clarifies provisions about:
    - various types of flexible leases and their impact on participation in DCP
    - bonus payments to landowners

Disposal Date	Distribution
October 1, 2007	State Offices; State Offices relay to County Offices

1 Overview (Continued)

B Purpose (Continued)

- reminds State and County Offices that:
  - tenant and landowners **must** provide FSA with DCP payment shares
  - using locally-developed or unauthorized forms is prohibited.

2 Current Regulations About DCP Division of Payment Shares

A Introduction

7 CFR § 1412.504 regulations provide the following provisions about lease types applicable for DCP purposes. See 1-DCP, paragraph 370.

Type of Lease	Definition
Cash	A cash lease provides only for a guaranteed sum, certain cash payment, or a fixed quantity of the crop. **Examples:** Cash, pounds, or bushels per acre. **Note:** 1-DCP, subparagraph 370 E provides that a fixed or standing commodity payment is the payment a tenant or operator provides a landlord for using the land and the landlord’s reduced risk on the crop, including the following: • a fixed amount of production, such as 10,000 bushels or pounds • an amount of production per acre, such as 40 bushels or pounds per acre.

Share	A share lease contains provisions that require:
	
	• 1 or a combination of the following:
	
	  • payment of rent based on the amount of crop produced
	  • proceeds derived from the crop
	  • interest the producer would have had, if the crop had been produced
	
	• the greater of a guaranteed amount or share of the crop or crop proceeds
	
	• both a:
	
	  • guaranteed amount, such as a fixed dollar amount or quantity
	  • share of the crop proceeds.

2 Current Regulations About DCP Division of Payment Shares (Continued)

B Foundation for Policy on Combination Leases

During the implementation of the Agricultural Market Transition Act, concerns were raised by OIG that a lease that provides for a portion of the crop proceeds allows landowners to receive Government payments that were not attributed accordingly for payment limitation purposes. OIG found that in many cases, these "combination" leases actually resulted in a crop share unless disaster severely impacted production.

Based on this concern, a task force was convened with representatives from States where combinations leases were prevalent and recommendations were made to change the regulations to provide that all leases providing both a guaranteed amount and a share of the crop or crop proceeds, including leases that provide for the greater of a guaranteed amount or share of the crop or crop proceeds, would be considered share leases. The regulations were amended, the policy became effective for FY 1999, and those provisions still apply for DCP.

The regulation states, "If a lease contains provisions that require the payment of rent on the basis of the amount of crop produced or the proceeds derived from the crop, or the interest such producer would have had if the crop had been produced, or combination thereof, such agreement shall be considered a share lease."

3 Flexible Leases

A Introduction

Using flexible or variable leases has become increasingly attractive to tenants and landowners due in part to fluctuating market prices. The conditions set forth in the lease can vary significantly, but many seem to fall into the following categories:

- rental rate is based gross crop value
- base, or minimum, cash rental payment plus the landowner receives a share of the gross crop revenue in excess of a certain base value
- rental rate is based on a fixed quantity with a fluctuating or future price.

DCP regulations about the applicability of various types of leases are **not** being amended to address issues about flexible leases. The remainder of this paragraph is intended to clarify how using flexible leases impacts DCP and other program areas.

3 Flexible Leases (Continued)

B Flexible Leases Based on Performance of the Farm

If the terms of the lease stipulate that the rental payment is based specifically on the crop produced or the crop proceeds, **program regulations provide that the arrangement shall be considered a share-lease agreement** for DCP purposes.

In share-lease situations, neither the landowner nor the tenant is eligible to receive 100 percent of the DCP payments for the applicable farm. Program regulations require that all producers sign CCC-509, agreeing to the payment shares.

These types of leases may not result in the landowner actually receiving a percentage of the crop grown; however, if the rental payment is based on actual production, these leases meet the **combination lease** definition according to 1-DCP, paragraph 370. As such, the shares **must** be designated accordingly on CCC-509 by the tenant and the landowner.

C Flexible Leases Based on External Factors

Some flexible or variable lease agreements provide that the rental payment is based on a set amount of production based on a future market value, not associated with the farm's specific production. **Program regulations provide that this type of arrangement shall be considered a cash-lease situation** because the rental payment is **not** contingent on the actual production of the crop or the crop proceeds.

Example: A lease states, "The annual rental payment is $150 per acre, but in the event that average corn yield **for the county** exceeds 170 bushels and/or the average cash price at the local elevator for the months of September, October, and November exceeds $3 per bushel, the rent per acre shall be $175 per acre." This lease would be considered a cash lease because the bonus payment is not tied to a specific yield on the farm nor the price received for that specific production.

In cash-lease situations, the tenant is eligible to receive 100 percent of the DCP payments for the applicable farm, provided all other program eligibility requirements are met.

3 Flexible Leases (Continued)

D Impact of Flexible Leases on DCP

CCC-509 Appendix provides that "each producer must provide a copy of their written lease to the county committee and, in the absence of a written lease, must provide to the county committee a complete written description of the terms and conditions of any oral agreement or lease."

DCP regulations and provisions do not prevent tenants and landowners from taking advantage of the various types of leases available in order to adjust for the changing market conditions. However, the conditions set forth in the lease will determine whether the arrangement is considered a share-rent or cash-rent situation for **DCP program participation** as specified in subparagraphs B and C.

State and County Offices shall ensure that producers are fully informed of DCP program participation requirements so producers can designate their shares properly on CCC-509. State and County Offices **shall not** make recommendations or compute DCP payment shares based on the lease agreement that is executed.

It is the producer's responsibility to make decisions for their farming operation and to comply with these requirements in order to meet DCP program eligibility requirements by designating their shares appropriately on the CCC-509.

COC, or their designee, shall review the shares designated on CCC-509 and applicable lease documentation to:

- determine whether the payment shares are reflective of each producer's interest in the base acreage based on the conditions of the lease agreement
- ensure the interests of tenants and landowners are protected according to 7 CFR Part 1400 and 1-DCP, paragraph 355.

If shares designated on CCC-509 do not meet these requirements, CCC-509 shall be disapproved and producer shall be notified of their applicable appeal rights according to 1-APP.

Further, the requirement that combination leases be considered share leases **for DCP purposes** does not require or force the landowner to participate in DCP. The landowner shall be required to sign CCC-509; however, the percentage of the payment attributable to the landowner shall not be issued unless all eligibility requirements have been met. The tenant's **eligibility to participate** is only impacted if the landowner does not sign CCC-509.

3 Flexible Leases (Continued)

E Impact of Flexible Leases for Other Program Purposes

7 CFR § 1412.504 provisions are applicable to DCP and do not apply to other programs unless specifically stated in the regulations for that program. Although DCP regulations require DCP payment shares to be designated between the landowner and tenant for combination lease situations, those regulations may not apply for other program purposes or other processes.

For example, a tenant may operate 100 percent of the land associated with a farm and retain ownership of the crops grown. Therefore, the shares reported on FSA-578 would indicate 100 percent. However, in a combination lease situation, shares must be designated to the tenant and the landowner. As a result, the shares on FSA-578 and CCC-509 would be different.

This is acceptable, because the terms of the lease agreement require that CCC-509 shares be designated between the landowner and the tenant. Similar issues may arise when producers file their farm operating plan and apply for loan deficiency payments.

COC's and County Offices shall:

- ensure that producers are fully informed of the applicable program provisions

- ensure that the applicable program provisions have been met before approving applications for payment for the applicable program

- **not** simply compare the shares on CCC-509 to the shares designated on FSA-578, or other program documents, to determine if the shares claimed for the applicable program are accurate.

F Example 1

In this example, the lease agreement specifies that the cash rent is based on a share of the gross revenue of the crop proceeds. The rental amount is equal to $142.80 per acre based on the following variables:

- cash rent is equal to 40 percent of the gross crop value
- the actual yield is 170 bushels per acre
- the actual price is $2.10 per bushel.

While the landowner does **not** actually receive 40 percent of the crop produced, this lease shall be considered a share lease for DCP purposes because the rental amount is based on a share of the crop proceeds.

3 Flexible Leases (Continued)

G Example 2

In this example, the lease agreement specifies that there is a base, or minimum, cash rent amount that must be paid, but the landowner receives a share of the gross revenue in excess of the base value. The rental amount is based on the following variables:

- base, or minimum, cash rent is $100 per acre
- additional rent is 50 percent of the gross revenue in excess of $250 per acre
- the actual yield is 52 bushels per acre
- the actual price is $6.50 per bushel.

In this example:

- gross revenue is equal to $338 per acre (bushels per acre times the actual price)
- the revenue in excess of the base is $88 ($338 minus $250)
- the additional rental payment is $44 ($88 times 50 percent)
- the total rental payment is $144 ($100 plus $44) per acre.

While the landowner does **not** actually receive 50 percent of the crop produced, this lease shall be considered a “combination”, or share, lease for DCP purposes because the lease agreement includes a guaranteed amount and an additional amount based on a share of the crop proceeds.

H Example 3

In this example, the lease agreement specifies that the cash rent is based on a fixed number of bushels; however, the price is based on the value that will be set on a future date, but it is not based on the actual price received by the producer. The rental amount is based on the following variables:

- the fixed number of bushels is 55 bushels per acre
- the actual price is the price at the local elevator on December 1.

This lease shall be considered a cash lease for DCP purposes. Although, the rental payment amount cannot be determined until the price is known on December 1, the rental amount is **not** tied directly to the crop or the crop proceeds.

4 Cash Rent "Bonus" Payments

A Introduction

Questions have been raised about how payment of cash "bonuses" to landowners impacts DCP program eligibility. Tenants entering into agreements with landowners for the 2007 contract period may be considering paying landowners a "bonus" payment for 2006 leases because of higher then expected yields or increased market prices.

B Impact on DCP

7 CFR Part 1412 regulations outlined in subparagraph 2 A, address the various lease definitions based on the terms of the lease. However, these bonus payments may or may not be included in the provisions of the original lease executed between the tenant and the landowner. The payment of a bonus to a landowner, in itself, is **not** a violation of DCP regulations.

Note: If the bonus payment is included in the lease agreement, COC's shall follow the provisions of paragraph 2 and 1-DCP, paragraph 370 for determining the type of lease agreement that is applicable.

However, the regulations include requirements that CCC:

- ensures that the fair and equitable treatment of producers
- determines that payment shares shown on the contract do **not** circumvent program provisions.

COC's, or their designee, shall follow the provisions of 1-DCP, paragraph 355 before approving CCC-509's for the 2007 contract period to ensure the interests of tenants, sharecroppers, and landowners are protected.

5 Cash Rent Certification Statements

A Introduction

Notice CM-538, issued May 2, 2006, reminded State and County Office that using locally developed forms is prohibited. Recently, a number of cash rent certification statements developed by County Offices have been submitted to the National Office, many of which were signed by producers after May 2, 2006.

B Privacy Act and Information Collection Procedures

As specified in Notice CM-538, any document that collects data from a producer, regardless of whether the producer's signature is required, is subject to the Privacy Act and Information Collection Procedures.

To adhere to the requirements of the Privacy Act and Information Collect Procedures, **all** forms, worksheets, and documents developed by State or County Offices that are used to obtain information **must** be submitted to National Office for review and official clearance.

C Using Cash Rent Certification Statements

1-DCP, paragraph 390 E provides that tenants can provide a written statement certifying that they have a cash lease for a farm and are authorized to receive DCP payments. This provision is provided as an alternative option to obtaining the landowners signature on CCC-509's.

However, many County Offices have developed forms for both the tenant and landowner to sign specifying that the tenant is cash leasing all, or a portion of, the applicable farm. Using County Office developed documents violates the Privacy Act and Information Collection Procedures in that the County Offices have developed forms require signatures that could otherwise be obtained on CCC-509.

The cash rent certification allows tenants to provide a written statement outlining the conditions of the lease arrangement with the landowner. COC's shall use the written statement information when determining whether CCC-509 should be approved. County Offices shall **not**:

- advise tenants as to the language that should be included in the cash rent certification statement other than to inform producers wishing to provide a cash rent certification statement that the terms of the lease arrangement should be documented

- develop or use State or County Office developed forms, worksheets, applications, and other documents other than those issued and/or cleared by the National Office.