

RENTAL ARRANGEMENTS FOR PROGRESSIVE FARMING

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PREFACE

This publication was developed by the Southern Farm Management Extension Committee in response to the many questions raised by Southern farmers concerning rental contracts. It suggests provisions to include in the rental contract to permit and encourage better farming on Southern farms.

A companion publication, "Determining the Rent in Share and Cash Rental Arrangements," suggests methods of determining fair rental rates.

This publication is based largely on unpublished research in rental arrangements, performed at North Carolina State College. The manuscript was written by C. B. Ratchford, who participated in the original research and checked the findings against results of other studies of rental arrangements. Mr. Ratchford is in charge of Extension Farm Management and Marketing work at North Carolina State College.

The responsibility for final development of this publication was assigned to a farm tenure subcommittee of the Southern Farm Management Extension Committee. The subcommittee was composed of M. C. Rochester of South Carolina, Chairman W. L. Gibson, Jr., of Virginia; C. B. Ratchford, of North Carolina; and E. P. Callahan of the Federal Extension Service Staff. In carrying out this assignment, the subcommittee had the benefit of many valuable suggestions from other members of the Committee.

It should not be overlooked that the arrangements under which this publication was developed were made through cooperation of the directors of the Extension Services of the Southern States, the Farm Foundation, and the Extension Service of the U. S. Department of Agriculture. The publication was approved and published jointly by the Extension Services of 12 Southern States.

DAVID S. WEAVER, *Administrative Advisor*
Southern Farm Management Extension Committee

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D. S. Weaver, Director
State College Station, Raleigh, North Carolina



Rental Arrangements For Progressive Farming

By

C. Brice Ratchford

Southern farmers realize that traditional farming systems and methods need to be changed.¹ They are adding tractors and equipment, pastures and livestock, changing farming practices, developing land and increasing the size of farms.

One of the barriers to these changes is existing rental arrangements. Most arrangements now in use were developed in an economy depending upon cash crops, cheap man labor and mule power. Today, most farmers are finding that these arrangements are not satisfactory. They are not adapted to an agriculture depending upon tractors, skilled labor, livestock as well as crops, and the whole array of changes now taking place in Southern agriculture. The purpose of this circular is to suggest changes in existing rental arrangements which will permit and promote desirable changes in farming.

Improvements Needed in All Leases²

TENURE SECURITY

Most rental arrangements are made for one year and terminate automatically at the end of the lease year. With such an arrange-

¹ This circular is based upon research performed in an area where the principal crops are tobacco, cotton, peanuts and corn. The recommendations may not apply in an area which has widely different farming systems and rental arrangements.

² These recommendations are intended for the consideration of landlords and tenants who are able and willing to assume the responsibilities they entail, to improve the farm business in the hope of increasing the net income of both parties.

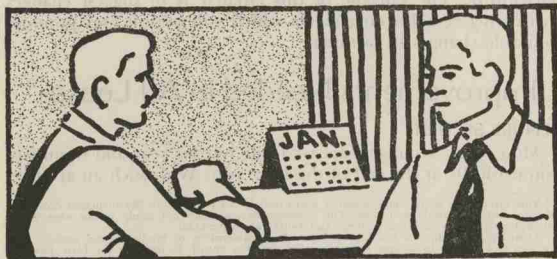
ment the tenant is not sure that he will be able to remain on the farm next year, if he so desires.³ The landlord is not sure that he will have a tenant to operate the farm during the year ahead, or that he can secure another tenant with the necessary skills.

Insecurity of tenure causes many undesirable farming practices. Modern farming cannot be conducted on a short term or annual plan. Where tenure is insecure, emphasis is placed on annual crops which can be planted and harvested within the term of the lease.

The tenant is not likely to invest his money or labor in long-lived crops such as pasture or alfalfa, in cover crops or in livestock when he is not sure that he will be allowed to remain on the farm long enough to secure the benefit from such investments. Also, the landlord is not likely to invest in facilities such as fences, a dairy barn or a poultry house if he is not sure that he will have a tenant who will use the facilities.

Security of tenure may be improved by agreeing that the lease will be automatically renewed for another year unless one of the parties notifies the other party three to six months before the end of the rental year that he does not want to renew it. A lease lasting from three to five years gives additional security. Neither the landlord nor the tenant may want to enter into a long term lease, however, until they know each other quite well. Many landlords and tenants find it desirable to first enter into a one year automatic renewable lease and later change to a longer term lease. Compensation provisions, discussed below, also add to security of tenure.

³The term "tenants," as used in this publication, includes croppers as well as share tenants and cash tenants. It should be recognized that adoption of the recommendations included in this circular may in some states legally change croppers to tenants.



FLEXIBILITY IN OPERATIONS

There is ample opportunity to change the farm plans under a one-year lease. Changes in plans for the coming year can be included in the lease for the coming year. When long term leases or one-year automatic renewable leases are used to add security of tenure, the desirable flexibility of the one-year lease may be lost.

However, the desired flexibility may be had in a lease which provides security of tenure by: (1) preparing an annual farm plan which becomes a part of the lease; (2) providing for termination of the agreement if the farm plan and other provisions of the lease are not carried out; and (3) providing for joint management by the landlord and tenant. The annual farm plan is strongly recommended.



COMPENSATION PROVISIONS

Compensation provisions can best be explained by two examples. Suppose the tenant seeds oats in the fall but the lease is terminated in December. Then either the landlord or the new tenant pays the departing tenant for the labor and materials he invested in the oats. This compensation provision works to the benefit of the tenant who is leaving and also to the landlord and incoming tenant.

There can also be compensation provisions in a lease protecting the landlord. Suppose for example that the lease specified that the tenant will maintain the same acreage of pasture and winter cover crops that was on the farm at the time the lease became effective. But when the tenant leaves the acreage of pasture and winter cover crops is less than at the beginning of the tenancy.

The tenant should pay the landlord the value of the deficiency.⁴

Compensation provisions are necessary from the standpoint of the tenant when major expenditures such as seeding pastures, fencing and land improvements are made during the term of the lease, if the tenant bears a part of the cost of these improvements. Compensation provisions are necessary from the standpoint of the landlord if the farm is highly developed and there are expendable improvements, such as permanent pastures, so that his investment will be protected.

Compensation provisions protecting both the landlord and the tenant are needed. The rate of compensation should be agreed upon before the improvement is made, whenever possible. An arbitration board can be used to determine the amount of compensation due either party in case agreement as to compensation cannot be reached.



DEFINITE, COMPREHENSIVE AND WRITTEN

The typical agreement includes little more than an understanding as to the acreage of cash crops, the division of crops and the amount of credit to be advanced by the landlord. The indefinite and incomplete rental arrangement leaves both the landlord and tenant uncertain as to many important points. This confusion tends to prevent either party from carrying out desirable practices.

Where there is a lot of uncertainty as to what is to be done, the usual result is that nothing is done. Disagreements arise from the indefinite, incomplete and oral leases now in use which result in misunderstanding and poor farming. Frequently landlords

⁴It is desirable to include a statement in the lease that the tenant will not pay for the reduced acreage in pasture and other seeded crops if the reduction is due to drought, flood or other causes beyond the control of the tenant.

complain that tenants are shiftless because they refuse to plant cover crops. Yet, when the matter is discussed with the tenants, they say that the landlord never indicated that he expected them to plant cover crops.

Tenants are often heard to complain that the landlord is not fixing up the house or putting in electricity as he promised he would when the agreement was made. Yet, after questioning the tenant closely it is found that the landlord never promised to perform these jobs.

Here is a more serious example of the result of an indefinite and incomplete lease. A share tenant was not dusting cotton in spite of heavy boll weevil infestation, because he and the landlord had not previously agreed upon how the cost of dust should be shared. The cotton was not dusted. The final result was that neither the landlord nor the tenant made expenses on the cotton. The same sort of thing has happened in thousands of cases.

The remedy for this kind of situation is a written lease which covers all important items of the farm operation. Items likely to cause disagreement and new developments in farming should be covered in detail. Items which should be covered in a good lease are listed on pages 18 and 19.

FULL EMPLOYMENT OF TENANT AND FAMILY

The typical tenant unit in many parts of the South does not provide year-round employment for the tenant and his family. A good income cannot be secured unless there is profitable employment for labor throughout the year. Underemployment of labor results from the small size of tenant units, and from the farming system which depends primarily on cash crops. The units are usually too small either to mechanize or to add an efficient live-



stock enterprise, both of which would permit more efficient use of labor.

Fuller and more efficient use of labor may be secured by several means. One method is to substantially increase the size of the tenant operated units—to two or three times their present size.⁵ This size unit would permit mechanization and the addition of livestock.

A second method is for the present acreage operated by tenants to be maintained or reduced with the landlord employing the tenants on a wage basis when the tenants are not employed in their own crops. In some cases non-farm employment may be combined with farm work. The method which is best depends upon the particular circumstances. If the tenant has managerial ability, has accumulated some capital, and the landlord is in no position to supply employment of a wage basis, increasing the size of the unit is the best approach. If the landlord is in a position to manage the farm and has crops and livestock of his own which make it possible to profitably employ wage labor, and if the tenant is not qualified to assume management, the second approach will generally yield the best returns to both the landlord and the tenant.

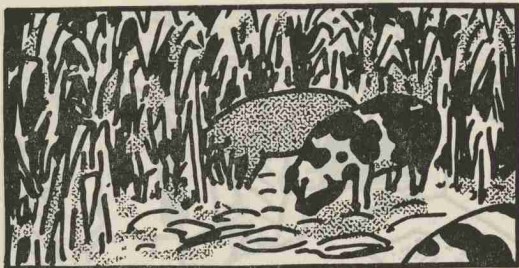


Additional Provisions for Share Leases

TENANT OWNS POWER AND EQUIPMENT

In many half-share tenant agreements the landlord furnishes power and equipment, an arrangement which hinders mechaniza-

⁵ The size of business can be increased in many cases without increasing the acreage through intensification. Even with a more intensive use of resources, an increase in acreage is usually needed to give full employment to the tenant and his family.



tion. Tractors are more economical than mules on large farms, primarily because of savings in man labor. The landlord with an agreement which calls for him furnishing equipment does not get any benefits from reduced labor requirements due to adding the tractor, since payment for labor is included in the half share of crops received by the tenant or cropper. Thus when a tractor and complementary equipment are added, the investment and power costs of the landlord may be increased while his labor cost is not reduced.⁶ Also landlords hesitate to let tenants use tractors and other pieces of equipment worth hundreds of dollars.

Tractors and equipment are primarily a substitute for labor. The party furnishing labor should also furnish equipment so that the substitution of capital for labor may take place. Such an arrangement also permits the tenant to become a property owner, which is quite desirable.

One barrier to tenants owning equipment is the lack of money or credit. Some landlords are selling tractors and equipment to tenants and taking a mortgage on the equipment. They say they would rather have mortgages on the tenant's tractor than to let the tenant use their tractor.

A second barrier to tenants owning tractors is the small size of tenant units. Most tenants cannot afford to own tractors until they can rent more land.

INCLUDES ALL ENTERPRISES

In share agreements in use in the South, the landlord usually shares only in the income from crops. The tenant is frequently

⁶ In the area where the research (on which this circular is based) was conducted, power costs were actually increased when tractors were added. This may not be true in all areas. However, the principle of the landlord not receiving large benefits from the addition of labor-saving equipment when he furnishes equipment in a share arrangement is valid in all areas.



permitted to produce a small amount of livestock and keep all of the income from the livestock. As the landlord receives no income from the livestock, he has little incentive to furnish buildings, pastures and other facilities needed for livestock production. If the tenant does not have security of tenure and is not protected by compensation provisions, he cannot afford to supply the needed facilities. Hence, the tenant is usually unsuccessful in his livestock venture because of the lack of facilities and because of the small size of the enterprise.

A share agreement should include all commercial crops and livestock enterprises on the farm or tenant unit. The landlord then has an incentive to provide the necessary land and facilities for conducting an efficient enterprise, whether it be livestock or crops.

COSTS SHARED IN SAME PROPORTION AS INCOME

In many share agreements either the landlord or the tenant furnishes the full amount of items such as fertilizer, seed and insecticides. In such cases, it will not pay the individual concerned to use as much of these items as would be profitable from the standpoint of the farm as a whole. For example, if the arrangement calls for the tenant to furnish all of the fertilizer, but he receives only half of the returns, he will not be inclined to apply as much fertilizer as he would if he received all of the returns or paid only half of the cost of the fertilizer.

Successful forage and pasture production in the South requires extremely high applications of fertilizer and at least part of the returns from fertilizer are deferred for several years and are much less certain than returns from fertilizer on the cash crops. Unless the cost of materials on the pasture and forage crops are shared

in the same proportion as income, a desirable amount of fertilizer will not likely be applied. The same principle applies to all types of materials and practices.

The easiest way to secure the desirable quantity of any item used in production is to share the cost in the same proportion that income is shared.

OPTIMUM INPUT OF UNSHARED COSTS

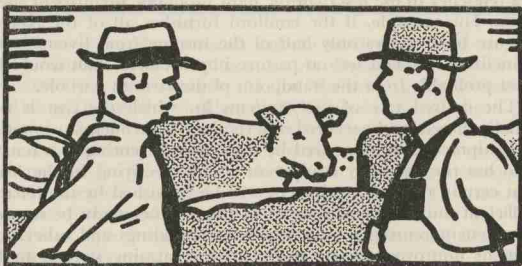
Share leases usually provide for the tenant to furnish all the labor and sometimes all the equipment and the landlord furnishing all land, buildings and permanent improvements and housing. When the cost is not shared but the income is shared, there is a tendency to use less than the most profitable quantity of these items. For example, if the landlord furnishes all of the cost of pasture but receives only half of the income from livestock, he is inclined to spend less on pasture improvement than would be most profitable from the standpoint of the farm as a whole.

The desired rate of use of items for which the cost is not usually shared can be secured in several ways. An adequate amount of equipment can be assured by the landlord renting to a tenant who has the necessary equipment or by specifying in the lease that certain types of equipment will be furnished by the tenant. Sufficient buildings and permanent improvements can be secured by a tenant renting a farm which has buildings and other permanent improvements necessary for the farming systems to be followed, or by reaching an agreement with the landlord when the lease is being prepared that certain buildings and improvements will be provided.

The optimum quantity of semi-permanent improvements such as pastures may be secured by sharing the costs of the improve-



ment. But the sharing of improvement costs should not be considered unless compensation provisions are included in the lease. The optimum application of items such as labor and management can be secured through penalty or bonus provisions or by sharing labor costs beyond a certain limit. For example, the landlord can prescribe a bonus for the tenant if yields are above a certain level, or if more than a certain number of hogs per sow are raised during the year. An example of sharing labor costs is the landlord paying for a share of the cotton picking. The whole problem is simplified by keeping the number of items for which the cost is not shared to a minimum.



LIVESTOCK OWNED IN SAME PROPORTION AS INCOME SHARED

Some landlords have entered into livestock share agreements in which the ownership of livestock was vested in the landlord. Reasons for this arrangement are (1) the tenant does not have the capital to purchase a share of the livestock; and (2) the landlord wants to retain ownership of the livestock upon termination of the lease.

Several difficulties are encountered when livestock is not owned jointly. First, there is an obstacle to expanding the size of the livestock enterprise. For example, suppose the tenant receives a share of the income from milk but does not own part of the livestock. The tenant objects to using some of the milk to raise replacements or additions to the milking herd, but insists that the landlord buy additional cattle which he may not be able or willing to do. Second, the tenant does not have sufficient incentive to properly manage the livestock. If the cattle belong to the

landlord, the tenant may not feel it necessary to call a veterinarian in the middle of the night if an animal is seriously sick.

These difficulties are avoided when livestock is owned jointly. The livestock should be owned in the same proportion as income is shared. Lack of funds on the part of the tenant can be overcome by the landlord selling the tenant part interest in the livestock and taking a mortgage on the livestock. Arrangements can be made to repay the loan out of the income from livestock and other enterprises.

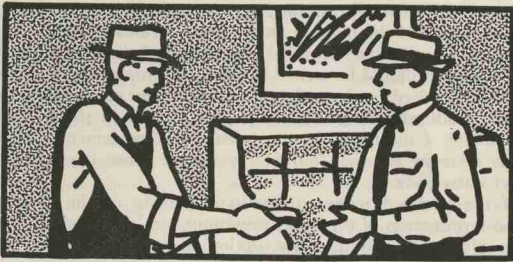
If the landlord wishes to retain ownership of the livestock upon termination of the lease, provisions can be included in the lease giving the landlord first option to purchase the tenant's share of the livestock upon termination, or vice versa.

MANAGEMENT RESPONSIBILITIES SHARED

In many agreements the tenant supplies little or no management. Under such an arrangement the level of management is less than desirable even for the production of crops and certainly far below the level necessary for the production of livestock. The level of management is lower than desirable because the landlord supplies most of the management but gets only a share of the income. Also, it is impossible in many cases for the landlord to supply the detailed management desired when there are several tenants located over a fairly broad geographic area.

Such managerial decisions as determining the farming system should be made jointly. Others such as when to buy and sell should be made by the better informed party. The tenant who is on the farm is often in the best position to make day-to-day management decisions such as determining when to plow and plant, when to call a veterinarian and most other daily decisions.





FAIR RENT

Much dissatisfaction, which results in poor farming, arises from disagreements over the amount of rent to be paid. Investments in permanent improvements, livestock, expensive equipment and conservation measures depend upon a mutual feeling that rental arrangements are fair. Also the ability of both parties to make additional investments depend in part on a fair division of income.

Income should be divided in the same proportion as costs are shared. For example, if costs are shared 40-60, the income should be shared 40-60. In planning the division of income, however, it must be remembered that the method of sharing costs affects the total returns, and also that costs include non-cash contributions such as labor, land and management as well as cash costs. For a discussion on determining fair rental rates, see Southern Farm Management Extension Publication No. 4.

Additional Provisions for Cash Leases

FLEXIBLE RENT

Practically all cash leases specify a single rental, such as \$10.00 per acre regardless of the number of years for which the lease lasts. If prices fall or yields are low, such a rent may be too high from the standpoint of the tenant. If prices rise or yields are high, it may be too low from the standpoint of the landlord. Hence, both the landlord and tenant hesitate to enter into long term leases.

A flexible cash rent should be provided which fluctuates with economic conditions and with weather conditions. For adjusting the rent as economic conditions vary, the rent is adjusted on the basis of some agreed-upon index. For example, assume that the

rent in 1951 is \$10.00 per acre and the parties have agreed to adjust the amount of rent as the parity ratio varies. If the parity ratio rises 10 per cent in 1952, the rent would then be \$11.00 for 1952.

The rent can be adjusted to account for varying weather conditions by varying the rent as crop yields for a geographic area vary. For example, the average yield for cotton for county (X) is 250 pounds. If the yield for the whole county for a certain year drops to 200 pounds per acre, the rent is reduced 1/5. If yields should rise to 500 pounds for the county as a whole in a given year, the rent would be twice the amount paid for the base year.

Flexibility to account for varying weather conditions may be difficult to achieve because yield data for a given area may not be available. No difficulty will be encountered in varying rent as the prices vary. A number of indices which could be used in adjusting cash rental rates are published by the U. S. Department of Agriculture and the state agricultural colleges.

SEPARATE RENT FOR LAND AND IMPROVEMENTS

Practically all rental arrangements provide for a single rental for the entire farm. A single rental will not likely bring forth the improvements such as good pastures, buildings and a good house for the family. For example, landlords are not likely to supply improved permanent pasture for a cash tenant unless a separate rent is paid for the permanent pasture.

The landlord either feels that the single rental is not sufficient to pay him for establishing pasture, or he feels that the same rent could be secured without seeding permanent pasture. Separate rents are needed for at least three groups of items: (1) land and usual buildings such as tobacco barns and cotton houses; (2) the dwelling and other privileges furnished the tenant such as fuel wood; and (3) improvements such as pasture, fencing and buildings constructed for single livestock enterprises such as poultry houses.

Separate rentals are not needed where the tenant makes the permanent improvements and is protected with security of tenure and compensation provisions.

FAIR RENT

A recent study in North Carolina indicates that most cash rental rates are quite low. Cash rent should provide the landlord a net income at least equal to that which could be secured if the farm was sold and the money invested in non-farm property such as

farm mortgages or bonds. For the landlord to earn a net return equivalent to that which he could earn on farm mortgages, the rent must include interest on the value of the farm plus taxes, depreciation on buildings and other improvements, maintenance costs, insurance on buildings and the value of the landlord's resources used by the tenant, such as fuel wood.



Suggested Types of Arrangements

Either a cash or a share lease can permit securing maximum income from a farm for the landlord and the tenant. It is obvious from the preceding discussion that it is easier to prepare a good cash lease than it is to prepare a good share lease. Under at least two conditions, however, the share lease may be more desirable. First, if the tenant lacks managerial ability, the managerial ability of the landlord may add materially to the farm income. Second, the tenant may be limited in capital and unless the landlord shares in the ownership of livestock and bears a share of expenses the optimum amount of capital and materials may not be supplied. Also, if the landlord is participating in the business the tenant may be a much better credit risk to lending agencies.

A share-cash agreement has much to recommend it where a share lease agreement is not feasible but the tenant can supply livestock. In this type of agreement the so-called cash crops are share rented to the tenant. The land and facilities used in the production of livestock are cash rented to the tenant.

There are several advantages to such an agreement. First, some landlords indicate that they are afraid to allot facilities in addition to those used for cash crops since the tenant may not carry out

the production plan and leave the land and other facilities idle. The cash rent must be paid even if the facilities are left idle.

Second, some landlords either do not want to participate in livestock production or are afraid that the tenant will not provide the necessary labor and management to make the enterprise profitable. This objection is overcome by cash renting the land, improvements and facilities used in livestock production to the tenant.

Third, the tenant is given more freedom in selection of enterprises and practices on the cash rented than on the share rented land. This freedom appeals to many tenants and permits the tenant to select enterprises which use his special skills.

Fourth, from a practical point of view it is difficult for one to be sure that livestock products are divided fairly in a share agreement. Such difficulties are avoided if facilities for livestock are cash rented. Of course, the straight cash lease also has the same four advantages over the share lease.

Preparing the Lease

The lease, whether oral or written, expresses the terms of the rental arrangement between two parties. Every person renting a farm has a lease. The written lease is merely a written statement of the bargain that has been made in conversation. It puts in writing for the benefit of all parties concerned the same points which are, or at least should be, contained in an oral lease.

One of the great advantages of a written lease is that it helps both parties to be sure that they have discussed and agreed upon the more important points. It is no more binding than an oral lease if the agreement can be proven. The purpose of the lease is to permit and encourage profitable operation of the rented farm. The lease should be designed to make farming profitable and provide for a fair distribution of income. It should prevent conflict and avoid arguments which end in taking the case to court. The purpose of the lease is not to substantiate one side against the other in a court action but to prevent the need for court action.

From a legal point of view, a lease is a contract and the laws pertaining to contracts are generally applicable to the lease. Special modifications have been provided, however, because of the nature of farming.

The lease may be in any form. It should be simple and fully understood by both parties. Standard lease forms are available

from the U. S. Department of Agriculture and some of the state agricultural colleges. Landlords and tenants may find it preferable to prepare a lease which suits their particular case rather than using a standard leasing agreement. It will frequently be desirable for the landlord and tenant to secure the services of a lawyer in preparing the lease.

Provisions to be Included in Leases

The following items should be included in a lease:

a. A statement of the landlord's intention to lease the property and the tenant's acceptance of the proposal.

b. A description of the property under lease.

c. The term or period for which the contract is to be in force, including the dates on which the lease begins and ends.

d. A general plan of operation, which gives in general terms the farming system to be followed.

e. An annual farm plan, showing cropping and livestock systems, and production and conservation practices. In order to simplify the lease, a provision may be included in the lease for preparing an annual plan which becomes part of the lease.

f. An agreement as to the payment of operating expenses such as fertilizer, maintenance expenses such as repairs to buildings and fences, and conservation expenses such as liming, ditching and terracing.

g. An agreement with respect to the division of the product, income or rent to be paid, and the time and place at which such division of the crop or payment is to be made.

h. Designation of the party furnishing workstocks, equipment and tractor.

i. Responsibilities of the tenant such as hauling out manure and maintaining ditches and terraces.

j. Responsibilities of the landlord such as furnishing wire, posts, fuel and housing.

k. Arrangements for credit.

l. Designation of management responsibilities such as selling, buying, culling livestock and day-to-day decisions such as when to plant and poison.

m. Business practices such as records to be kept, the party to keep records and the party paying expenses.

n. Compensation for the landlord and tenant. This section should be given in detail.

o. Arbitration provisions if desired. The best method for arbitrating disputes is to provide for a three-man board—one mem-

ber selected by each party and a third selected by the two already selected. The board can act as advisors or a statement can be included in the lease indicating that the decision of a majority of the board would be final and binding upon both parties except where a matter of law or fraud are involved. The arbitration board can also determine the amount of compensation due either party.

p. Termination provisions. It is important that the lease specify the disposition to be made of jointly owned livestock and supplies.

q. Reservations of the landlord and tenant. Reservations such as not permitting the tenant to sublet part of the farm or plow up pastures should be included in the lease.

r. The signatures of the parties.

For additional information needed in making rental arrangements, see your county agent or write to your State Agricultural College.

For additional information, also see Southern Extension Farm Management Publication Number 4, Determining the Rent in Share and Cash Rental Arrangements.

Southern Farm Management Extension Committee

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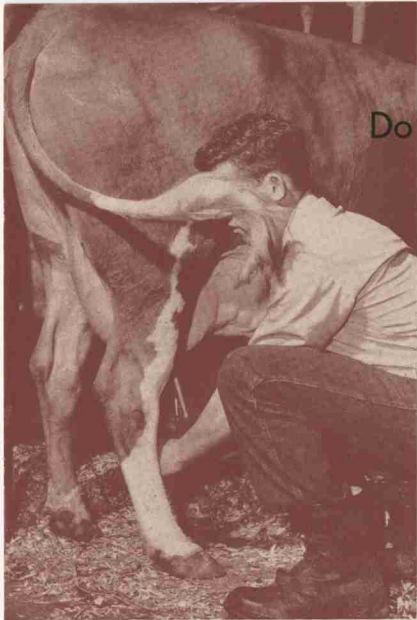
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Do You Kick The Cow or Kill The Bugs

Fighting flies with the only weapon at her disposal, Bossy has no idea of the anger she provokes. Sure, you're tempted to hit 'er back, but would that do any good? No, if you want results, you get out the spray gun and go after the bugs.

And therein lies the secret of getting along with your landlord or your tenant. Owners gripe at their tenants for letting the farm run down, and tenants grumble about landlords who take too big a share of the crop. Actually the real culprits are often "the bugs" in farm leases.

Some of "the bugs" common in farm leases are:

- (1) An oral agreement.
- (2) A one year lease without automatic renewal provisions.
- (3) An unfair rent.
- (4) Provisions which prevent improvements on the land and in the home.

Other "bugs" and means of destroying them are included in this and companion publications.

The farm program in this publication offers just as much to the tenant farmer as to the owner. But to put these adjustments into effect, landlords and tenants must bring their leasing agreements up to date.

So before you take your spite out on your landlord or your tenant, be sure you've got all "the bugs" out of your leasing arrangement.