

## RURAL LEASING AND SHARE FARMING: CONTRACTUAL TRENDS AND OPTIONS

John McMullan and Angela Vaccari, 20 July 2012<sup>1</sup>

*Rural Australia has a long history (good and bad) of negotiating informal handshake agricultural tenancy arrangements. Various factors are now driving change towards more formalised written contractual forms. Every farm is different and likewise every contract. The legal vehicle should reflect the value and importance of the farm, and continue from generation to generation.*

Last year's floods have, yet again, highlighted the need for high-value rural properties to have proper commercial structures in place.

Rural Australia has a long history of negotiating informal handshake agricultural tenancy arrangements. Unlike the USA, UK and New Zealand, Australia has been slow to adopt more formalised written contractual forms. Except for New South Wales, which has the *Agricultural Tenancies Act 1990*, there is no *specific* agricultural tenancy legislation in Australia regulating the rights between agricultural landowners and their tenants and sharefarmers.

Importantly, there are generational changes affecting the ownership and operation of family farms. The land inheritance pattern in Australia has shifted away from the tradition where the farm was left to the eldest son. Share farming and agricultural leasing is increasing and more farmers have, and will have in the future, tertiary farming qualifications. Farm assets and the business of farming are becoming more complex, with large amounts of capital and investment involved in big business farm models.

The driving factors now include the following:

1. The farm needs to be in a structure (unit trust/company) so that the income can be transferred or left to all of the potential stakeholders, but without diminishing the worth of the asset by breaking up the land or the business.
2. The farm business may incorporate commercial arrangements such as share farming, farm leasing, stock financing, direct selling etc.
3. The farm business needs to be maximised through systematic involvement with rural consultants, agricultural experts, and land and equipment financing to maximise crop and grazing income.

There is an increasing need for farms to be treated like other high-worth corporate ventures. The legal arrangements should reflect the value and importance of the farm to the family, and continue from generation to generation.

At a minimum, farm owners should structure the farm asset (the land, improvements, equipment and the business) so it can be conveniently and tax effectively enjoyed (by the children, or for sale or financing) without breaking up the land itself.

The contractual vehicle should be tailored on a farm-by-farm basis. Where farmland is to be cropped, who owns the crop if it is not ready to be harvested at the expiration of the lease term? Does the

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tenant have a right to re-enter the land and harvest the crop?<sup>1</sup> If the farm lease includes residential accommodation, what additional rights and obligations (if any) might apply under the residential tenancies legislation?<sup>2</sup>

These sorts of issues may, if overlooked, lead to a breeding ground for disputes.

Where farmland is to be leased, the lease document should, in plain English, spell out and define<sup>3</sup> the detailed tenant obligations, including, for instance, using the landlord's plant and equipment, fixtures, paying for water and other services, obtaining and maintaining licences, fertilizing obligations, chemical use, grazing limits,<sup>4</sup> re-sowing, land clearing,<sup>5</sup> vermin control, fire prevention, disease control, fencing standards and condition report,<sup>6</sup> insurances, timber/soil removal and replacement etc. The lease should record how rent is to be calculated and reviewed, and record the deal on the maintenance of the land, including regular landlord inspections, a photographic record commencing from the start and updated throughout the lease term, and the obligation to return the property in an acceptable condition. These may seem tedious, yet they are critical.

Where land is to be share farmed, the share farm agreement has to spell out and define what is paid for and/or owned by the share farmer or by the landowner, including, for instance, the types of stock or crop, farm labour, operating plant and equipment, marketing, land rates, water, fertilizer, fencing standards and condition report etc, and, the most critical detail, the sharing of the farm income. Again, the share farm agreement should spell out and define the share farmer's land protection obligations (using the landowner's plant and equipment, fixtures, paying for water and other services, and, again, the deal on the maintenance of the land, including regular landlord inspections, a photographic record commencing from the start and updated throughout the lease term, and the obligation to return the property in an acceptable condition.

Record keeping is critical, for example, detailed records must be available for the landlord regarding chemical used on livestock and chemical application on crops and pastures.

Prior to entering into a lease or share farm agreement, the landowner should also ensure that the condition of the land (including capital improvements, plant and equipment etc) is acceptable to the tenant as well as any other requirements imposed at law, including, for instance, occupational health and safety standards and auditing, the state of shearing plant, silos, sheds, yards, fences, gates, waterways, windmills, the extent of thistles and other noxious weeds etc. The landowner should, in addition to any other requirements imposed by authorities/legislation, notify the prospective tenant/share farmer about animal health issues and disease risks (past, present and suspected) on the land and adjoining areas, such as lice, footrot, Ovine Johne's Disease (OJD) etc.

When it comes to the resolution of agricultural tenancy disputes, litigation can be very costly and time-consuming. A number of Alternative Dispute Resolution options can be included in a lease or share farm agreement, which are often relatively quicker, less expensive and less formal than adversarial court/tribunal processes. Mediation is one ADR option, involving the assistance of a neutral third party to negotiate a decision about a dispute. Some prefer (others may not agree) to also include an Expert Determination arrangement, listing agreed farm experts, to decide (if needed) on certain farm/land issues under the lease and share farm agreements, for instance, the adequacy of condition reports, land management plans, land treatment and fertilizing obligations, limits on grazing or stocking rates (including a stocking policy during droughts), maximum proportion of area to be cropped, crop rotations, sowing and ground cover obligations, fencing standards and condition reports etc.

The structuring of farms and the commercial agreements relating to the business of farming is, irrespective of the history of handshake arrangements (good and bad), certain to follow new trends, skills, complexities, and aims of farming land as a business operation.

The farm is, typically, valued in the millions of dollars, and in many instances, it is the sole asset and source of income of the family. The commercial/legal structures and arrangements need to reflect the value of multi-million dollar farm assets.

Every farm is different and likewise every contract.

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<sup>1</sup> See, for example, *Hohn v Mailler* [2003] NSWCA 122 where the New South Wales Court of Appeal determined whether a clause in a fixed term agricultural lease altered the landlord's right to harvest sorghum planted by the tenants approximately one month before the expiration of the Lease term.

<sup>2</sup> In Victoria, the *Residential Tenancies Act 1997* (Vic) does not apply to residential tenancies **included** in the farm lease for a range of agricultural purposes: s 11.

<sup>3</sup> Some parties like to include a **Glossary of Agricultural Terms** in a schedule to their agreement. See, for example, the University of Adelaide, *Glossary of Australian Agricultural and Farm Business Management Terms* <<http://www.agwine.adelaide.edu.au/agribus/agribus/resources/glossary/>>.

<sup>4</sup> Parties may decide to include a schedule of **Dry Sheep Equivalent (DSE)** to define the permissible Stocking Rate. DSE is a measure frequently used to compare the feed requirements of different classes of stock or to assess the carrying capacity and potential productivity of a given farm or area of grazing land. DSEs can be particularly important during periods of drought or feed shortages. The definition of a DSE for different livestock classes may be set out in DSE Rating Tables contained in a schedule.

<sup>5</sup> Sowing Limits/Groundcover obligations may be set out in a schedule, whereby, the Tenant may, for instance, be required to ensure groundcover is maintained above a minimum level (eg. above 70%) by removing livestock from pastures and crops once groundcover reaches 70%.

<sup>6</sup> The types of fences on a property often vary dramatically. There is no such thing as a "standard fence". In addition to identifying the various fencing types and maintenance standards, parties may wish to nominate one or more agreed Fencing Experts in a schedule to their agreement.