Share Farming “A new land access option”

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SUMMARY

Share farming is the term used to describe an arrangement where two parties, the landowner and a share farmer, carry on separate farming businesses on the same land without forming a partnership or company. Each makes separate contributions for example land, machinery, labour and expertise and takes a share in the produce or gross output. Likewise each party to the arrangement contributes their own costs of production. The share farmer and landowner keep their own accounts and calculate their own profits as separate and independent businesses, notwithstanding that each business is closely linked to each other.

The arrangement is not and cannot operate as a defacto conacre arrangement as both parties must share risks and rewards The details of a share farming arrangement are set out in a written legal agreement. As both individuals remain separate business entities they may continue to claim the Single Farm Payment, REPS etc, in their own name and also maintain their separate tax affairs as normal.

The appeal of the agreement to growers is that it allows a new way of accessing land which increases scale in a controlled manner. Properly managed, this increase in scale will reduce production costs through increased purchasing/ selling power and will lower machinery costs and reduce fixed costs per acre. For the landowner the share farming agreement offers the opportunity to leverage all the advantages attained by grower and also tap into the expertise of the grower to increase output. The increased output at lower costs increases the overall output benefit for both parties in the agreement.

All farmers and landowners should familiarise themselves with the agreement and assess whether it is a viable option for the future.

INTRODUCTION

The current price cost squeeze has resulted in low or negative margins for all tillage farmers. Economic survival with these lower margins necessitates scale to generate sufficient income. Up to now the options to acquiring scale was either purchase of land, long term leasing or conacre. Each option presents significant difficulties especially now that credit is scarce.

The capital required for land purchase renders this option unviable for most. Long term leasing is a reasonable option to attain scale and can have tax advantages for the land owner but access to a reasonable quantity of leased land has proved difficult. The long term nature of leasing allows longer term planning by the farmer it also locks the farmer into a fixed rental payment and in many cases the burden of this payment is prohibitive. Finally, most growers use conacre to attain scale. The longevity of the conacre system indicates that it can be successful but not for all and not every year. Over recent years the rental payments demanded from landowners, or the willingness of growers to pay high rental prices, has wiped out any chance of profits for the farmer in all but exceptional years.

Share farming offers land access where scale can be achieved at a sustainable level. Share farming can offer the advantages of longer term lease without fixed payments and similar flexibility of conacre while sharing some of the risks. Share farming is fully compliant with EU schemes (Single Farm Payments, REPS, etc.) which enable the land owner to claim all subsidies as before and continue to be classed as a farmer by Revenue (therefore retaining retirement relief's). Both the share farmer and the landowner benefit from increased scale through increased buying and selling power. In many cases the expertise of a specialised tillage farmer can improve yields and increase output on a share farm compared to returns attained before the share farming agreement.

SECTION 1

Share Farming: The Concept

Share farming is a contractual arrangement between two independent farming businesses where two people, a landowner and a share farmer, by adhering to certain principles, jointly farm the same area of land as separate businesses remaining separate and independent for accounting and tax purposes. The details of the arrangement are set out in a legal written contract. The landowner may continue to avail of the various National and EU support payments where the conditions of those schemes continue to be met.

The share farmer and landowner, on the basis of a budget (a planning tool), agree to divide the farm produce and fixed costs between them. Such a budget will allow the parties to agree, at the start of the arrangement, the percentages in which outputs and costs will be allocated as they arise during the course of operating the agreement. There is no guaranteed return to either party.

Each party is a risk taker. Following the distribution of outputs each party calculates their own profit and is responsible for his own tax.

An example share farming arrangement (described in Section 2) could involve two parties as follows:

(i) a landowner provides land, some material inputs, fixed equipment, major upkeep and repairs. He also provides some management and farming expertise.

(ii) a share farmer provides some material inputs, mobile machinery, his labour, management and farming expertise.

(iii) In the example outlined in Section 2 by participating in a share farming agreement the land owner increases his income by 25%. The share farmer generates an income of €7,800 after machinery costs and the grower has achieved an increase in scale.

When participating in a share farming agreement the following general principals apply:

- The landowner and share farmer are free to sell their share of the farm produce (e.g. grain, straw) as they feel fit.
- Each party is responsible for his own costs of production.
- Each party works out his individual profits following the distribution of the output.
- The share farmer and landowner share the enterprise risks.
- Both parties, the share farmer and landowner, are jointly responsible for planning the business annually, including cropping, rotations, stocking, breeding policy and purchase and sales.
- There should be no joint bank account or joint trading account. in operation
- No rent (i.e. a fixed sum) is paid for the land.
- A contractor hire cost is not paid to the share farmer for the use of his machinery (labour element is excluded).
- If registered for VAT each party is separately registered and account for their own VAT returns
- A landowner can choose to share farm all or part of his/her farm

How does share farming differ from a partnership?

In contrast to a partnership as specified in the Partnership Act (see appendix), the objective of a share farming arrangement is that, while both parties agree to cooperate, two separate businesses are carried on, where each person, the share farmer and landowner, calculates his/her separate profit from his/her separate gross returns and separate costs.

Therefore care has to be exercised by the parties to the share farming arrangement to ensure that the arrangement, on examination, cannot be construed as some other legal entity such as a partnership, a letting/leasing arrangement or that it does not come under the scope of employment legislation.

A written share farming agreement alone is not sufficient evidence of a proper share farming arrangement being in place. The carrying out of the practical arrangement has also, under examination, to comply with the principles of share farming. An arrangement that is found to operate as something other than share farming may give rise to serious legal, tax or EU/Government support scheme implications for the participants. Tax issues could arise e.g. under categories such as Income Tax, Capital Gains Tax, PAYE, VAT and special stamp duty relief for young qualified farmers. To guard against such default arrangements occurring, participants are strongly advised to ascertain sound professional advice/assistance when drawing up a share farming written agreement and afterwards to ensure that it is operated as described in that agreement.

How does share farming differ from a lease or conacre?

Leasing of farmland in Ireland normally involves a written lease for a fixed term of a minimum of one year or more with a fixed payment per acre (or per hectare) per annum for the leased area. Similarly conacre (11 month system) also requires a fixed payment per acre (or per hectare) as part of the agreement.

However, if a landowner and share farmer were to enter into a "so-called share farming arrangement" where the landowner is guaranteed a minimum payment per acre (or per hectare) then there is the possibility that such agreement could be construed as conacre.

In the event of the Revenue Commissioners or the Department of Agriculture judging that the arrangement is effectively conacre as opposed to share farming then the landowner will be deemed not to be farming the land. That could lead to serious implications which could give rise to withdrawal of benefits available to active farmers under the following headings:

(1) Tax: Assessment of income tax as a farmer, capital gains retirement relief or stamp duty relief for young qualifying farmers.

(2) Support payments: Current and future EU/Government support payments

EU/Department of Agriculture Support Schemes

Farmers who are involved in share farming can qualify as separate individuals under all three schemes provided that each party, the landowner and the share farmer, hold separate herd numbers or other identifiers, submit separate eligible land and meet all the other conditions of each scheme (Single Farm Payment, Compensatory Allowance Scheme Payments and REPS).

Table 1 Examples of typical DAFF support scheme scenarios are outlined below

Example	**Share Farmed land area**			
	Landowner claims		**Share-Farmer claims**	
	SFP	**REPS**	**SFP**	**REPS**
Example 1 Landowner brings land & entitlements	✓		✗	
Example 2 Landowner brings part of farm and entitlements (continues to farm rest of the farm land)	✓		✗	
Example 3 Landowner brings land, entitlements and is in REPS	✓	✓	✗	
Example 4 Landowner brings land, has no entitlements but is in REPS		✓	✗	
Example 5 Landowner brings land, has no entitlements and is in REPS Share Farmer brings entitlements	✗	✗	✓	

Taxation

Both parties maintain separate accounts and continue to be assessed as individual businesses for tax purposes. A share farming agreement can be developed between a VAT registered farmer and an unregistered land owner. A registered farmer must account for VAT on his supplies used to produce the crop and the unregistered landowner is not entitled to VAT deductibility and does not charge VAT on his supplies. Revenue has produced detailed examples of the procedures to deal with VAT which can be obtained from the Teagasc website www.teagasc.ie.

Typical agreement

An agreement should deal with a range of topics and where relevant specify how each item is to be dealt with. Teagasc can provide assistance in the development of an agreement, particularly the budget and profit share arrangements which are absolutely crucial to the success of a Share Farming arrangement. Contained within the share farming agreement developed by Teagasc are the following:

- Duration of the agreement

  The duration of the agreement is up to the participants and would typically be for a period of 3 to 5 years. A one year agreement is possible but may be too short as the drawing-up a share farming agreement involves time and effort and it hinders long term strategic (cost efficient) decisions.

- History of cropping, fertility and lime status

  Accurate information on recent cropping history and fertility status could have a considerable bearing on projected yields and returns during the share farming contract. Such information would also facilitate better husbandry and management decisions during the first few years of the agreement.

- Formation – The agreement should specify in detail what each party agree to provide in the arrangement.

  - The landowner provides, as a minimum, the land on which the share farming operation is to be carried out along with some management expertise. Details of the land including area and LPIS numbers should be specified in the agreement.
  - The share farmer typically provides machinery, labour, management expertise and, on rare occasions, entitlements to be used on the share farmed land.

- Division of the produce and farming subsidies

  The agreement should be clear on how farm produce e.g. grain is to be divided between the landowner and share farmer. Each party will be free to sell his share of the produce as he feels fit, however, by agreement the share farmer may by way of convenience sell the landowner's produce on behalf of the landowner and then pass on to him the amount received.

  If it is agreed to split the Single Farm Payments or other subsidies, then these will have to be drawn down by the relevant person, the landowner or share farmer. On receipt of the cheque the proceeds could then be divided between the two parties as set out in the agreement.

- Division/allocation of costs

  Costs fall into two main categories: variable and fixed. With the aid of a budget costs are agreed and it should be clearly established what costs are to be carried by each party at the commencement of the agreement.

- Variable costs such as fertiliser, seed and chemicals can be carried on agreed percentages e.g. a percentage of all the inputs could be paid for by the landowner and the remainder by the share farmer. Alternatively the landowner could for example pay for all the fertiliser and seed while the share farmer could pay for all the chemicals. The share farmer can leverage his purchasing power for all materials purchased.

- Fixed costs such as labour, insurance and repairs should be carried by the relevant parties. It would be normal for the share farmer to pay for all hired labour. The alternative being that he would be to do the work himself. Machinery repairs are likely to be paid for by the party who owns the machine and that in most arrangements will be the share farmer.

- Maintenance of buildings and maintenance work on the land

  The cost of building maintenance work and land upkeep has to be agreed between the parties. It could e.g. be agreed that the buildings and land should be maintained to the same standard as at the start of the agreement and that any cost associated with upkeep during the agreement would be carried by the share farmer.

- Penalties due to non-compliance with EU/DAFF support schemes

  Penalties for non-compliance with the various regulations can arise. Clarity on how such penalties are dealt with between the share farmer and landowner is essential to avoid disputes. Fairness and equity are important underlying principles that need to be adhered to.

  There are three types of situation that need to be addressed in the agreement as follows:

  - Penalties applied to a landowner because of non-compliance on land outside the agreement
  - Penalties applied to the share farmer because of non-compliance on land outside the agreement
  - Penalties applied to the share farmer because of non-compliance on the share farmed land

- Insurance

  As each business, the landowner and share farmer are farming as separate businesses it is imperative that each have their own insurances. Before entering into a share farming arrangement each party should consult with their insurer.

- Prevention and resolution of disputes

Having a well thought out agreement setting out the rights, obligations and responsibilities of each party as well as agreeing how the share farming is to be operated on an ongoing basis is a basic requirement. It is important that the share farmer and landowner are involved in the actual drawing up of the agreement: It is not sufficient to have an agreement drawn up by a third party without their input into all aspects of what is agreed.

- Death of a party

  Provision for what should happen in the event of death of one of the parties to the agreement is important for two reasons. Such an event would be traumatic for all involved and because there would be only one party left then lack of a roadmap in the agreement could add additional unwelcomed trauma.

- Dissolution of the agreement

  Aside from death, early dissolution of a share farming agreement could arise e.g. because of dispute, sickness or financial issues. Whatever the reason it would be wise to provide for such eventualities in the agreement.

SECTION 2

Share Farming in Practice

The following section will outline an example of a typical agreement and reasons for some of the divisions in costs and outputs. Outputs from the Teagasc crop share calculator are used to illustrate the divisions of costs/outputs and totals for each party

John Reilly, a medium to large tillage grower, has been working alongside his neighbour, Tom Byrne, for some time now. Tom is a mixed dry stock and tillage farmer who uses some of the grain and all the straw form the tillage enterprise in this drystock enterprise. He sells all excess grain green at harvest.

Over the years John has increased the amount of work completed for Tom on his 100 acres (40 hectares) of tillage land. At the moment John is carrying out primary cultivations, sowing and combining the 100 acres (40 ha) for Tom. Tom has reached a cross road with his tillage enterprise as yields are not where they should be and his remaining machinery is becoming unreliable. However Tom will retain his drystock enterprise and wishes to have some control over all his land.

The two farmers now wish to extend their relationship and enter into a Share Farming agreement for the 100 ac (40ha) of tillage with John as the Share Farmer (SF) and Tom the landowner (LO).

A vital part of any agreement is trust and this has build up over the past number of years between the parties. The next step is to decide on the cropping programme and construct a budget for the coming year.

Tom (LO) will supply land with entitlements for each acre (hectare) and this land is also in REPS. Tom will bring both the Single Farm Payment and the REPS payments into the share farming agreement. Tom will claim the Single Farm Payment and REPS and draw them down in his name as normal.

John (SF) will provide the machinery and expertise in growing the crops. Both John and Tom have separate accounts in the same merchant. John will use his power of purchasing to leverage the best prices for all the inputs. When inputs are purchased both John and Tom will be charged (through the separate merchant accounts) the agreed proportion of the cost. Any inputs bought outside the merchants will be purchased by John, who will in turn invoice Tom for his share of the purchase. John has agreed to sell Toms share of the grain, again leveraging his increased selling power. Figure 1 outlines the crop budget for 2010.

The spring barley budget 1 (on the left in Figure 1) outlines the production from Tom Byrnes farm before entering a share farming arrangement. Tom’s yields are modest (considering his land) and he buys material costs at the higher end of the pricing scale therefore material costs are higher than they should be.

Figure 1 Crop budget for the 100 acre farm (40 hectare) shared farm

Crop-Share Calculator Page 1: Costs and Returns per acre

T. Return/ac	Barley Spring	Barley Spring	
Landowner	166	209	
S Farmer		78	
Budget	1	2	

RECEIPTS *per acre*	Crop	Barley Spring	Barley Spring	
Area		100.0	100.0	
Yield		2.5	2.7	
Price		€110	€120	
Straw		€30	€36	
Other (Bonus, etc)				
		€305	€360	
EU/Government Support				
Single Farm Payment		€130	€130	
REPS		€50	€50	
Direct Payments (e.g. Protein, etc)				
Other				
		€180	€180	
	TOTAL RECEIPTS	€485	€540	
MACHINERY COSTS*				
Field operations		€120	€100	
Machinery Hire		€40		
Drying (per acre basis)			€21	
	TOTAL	€160	€121	
MATERIAL COSTS				
Seed		€26	€22	
Fertiliser		€68	€60	
Lime				
Chemicals:	Herbicide	€20	€15	
	Fungicide	€30	€25	
	Insecticides	€7	€6	
	Trace Elements	€5	€4	
	Other			
Other costs (Haulage/Interest, etc)		€3		
	TOTAL	€159	€132	
	TOTAL EXPENSES	€319	€253	
	Crop Margin	€166	€287	

Cells highlighted in light yellow require user input
Cells highlighted in gray are automatically generated

Both parties agree the land can return higher yields and John (SF) is confident he can reduce input costs (through better purchasing).

From budget 1 Tom is earning €16,600 from running the enterprise on his own. Considering his direct payments amounts to €18,000 on this enterprise Tom is clearly loosing money cropping the land.

The spring barley budget 2 in Figure 1 shows an increased return for the enterprise due to increased yield, higher selling price, lower material costs and lower machinery costs due to the increased scale of the John Reilly (SF).

The margin to each grower can be seen at the top of the crop budget for each grower. This is calculated based on the agreed distribution of costs and returns (see Figure 3). Under the new share farming agreement Tom Byrne (LO) margins has increased from €16,600 (€166 per acre) to €20,900 (€209 per acre), an increase of 25%. John Reilly (SF) sees a return of €7,800 (€78 per acre) for his labour/expertise after machinery costs.

Figure 2 Sensitivity Analysis of budget

Sensitivity Analysis per acre (add or subtract from crop budget in Costs and Returns)					
		Budget	1	2	
Yield			**Barley Spring**	**Barley Spring**	
Land owner	+/- 0.1 t/ac		**€11**	**€5**	
S Farmer	+/- 0.1 t/ac			**€7**	
Grain Price					
Land owner	+ €10/t		**€25**	**€11**	
S Farmer	+ €10/t			**€16**	

In Figure 2 a sensitivity analysis of each budget. Budget 1 shown the sensitivities when the land owner works on his own. Budget 2 shows how each parties margin per acre changes if the yield or price changes in either direction as part of the share farming arrangement.

The distribution of costs and returns between the parties are highlighted in figure 3.

Figure 3 Division of outputs and expenses

Crop-Share Calculator Page 2: Shared percentages of Costs and Returns

T. Return/ac	Barley Spring	Barley Spring	
Landowner	166	209	
Share Farmer		78	

See below for specific instructions

Buget	1		2			
	Barley Spring		Barley Spring			
RECEIPTS	**Landowner**	**S. Farmer**	**Landowner**	**S. Farmer**	**Landowner**	**S. Farmer**
Grain	***100%***		***40%***	60%		100%
Straw	***100%***		***100%***			100%
Other	***100%***			100%		100%
EU/Government Support						
Single Farm Payment	***100%***		***100%***			100%
REPS	***100%***		***50%***	50%		100%
Direct Payments (e.g. Protein, etc)	***100%***			100%		100%
Other	***100%***			100%		100%
MACHINERY COSTS						
Field operations	***100%***			100%		100%
Machinery Hire	***100%***			100%		100%
Drying	***100%***			100%		100%
MATERIAL COSTS ***per acre***						
Seed	***100%***		***100%***			100%
Fertiliser	***100%***		***100%***			100%
Lime	***100%***		***60%***	40%		100%
Chemicals: Herbicide	***100%***		***60%***	40%		100%
Fungicide	***100%***		***60%***	40%		100%
Insecticides	***100%***		***60%***	40%		100%
Trace Elements	***100%***		***60%***	40%		100%
Other	***100%***		***60%***	40%		100%
Other costs (Haulage/Interest, etc)	***100%***		***60%***	40%		100%

Explanation as to division of costs and outputs

1. Yields based on 5 year averages and potential yield of land
2. Grain price mix green/dried and €15 ton factored in for drying half the grain
3. As John Reilly (SF) owns and operates all machinery he bears all costs and these costs do not include labour i.e. not equivalent to local contractor charges
4. Where John Reilly (SF) buys fertiliser for the share farming agreement, he will invoice Tom Byrne for his share and also show this fertiliser as an export on his nitrates plan to comply with Cross Compliance
5. REPS split as additional work such as Linnet and margins affect practical farming
6. As part of this agreement Tom (LO) will retain 40% and all the straw for his livestock operation.
7. Tom (LO) will purchase all the seed and fertiliser (at the price obtained by John, the share farmer).

The total output from the share farming enterprise has increased the output from by €12,100.

Once both sides (and their legal and financial advisors) are happy with the agreement it is signed and then the partialities of the joint venture can begin. Tom will continue to claim his Single Farm Payment and REPS by submitting the relevant application forms as usual. Regular meetings will be held through the year to assess progress and deal with any financial matters arising. After harvest, or when it is deemed best to sell the grain and straw, both parties will sit down to complete the sharing of outputs, etc. Both will complete their own tax affairs (including VAT) as normal (as separate businesses). A new budget should be constructed for the following year as the cropping plan and prices expenses can change from year to year.

Conclusions

The share farming arrangement outlined here is a new concept to Irish agriculture and will work in tandem with conacre and lease agreements. The agreement offers new opportunities for growers to build a sustainable land area on which sound financial decisions can be made. The agreement also offers both parties the security of a well-structured and thought-out agreement which has a sound legal footing.

The basis of the agreement allows two parties to remain as independent businesses while combining resources to generate income. A Share farming agreement is:

- Flexible and will accommodate most situations
- A legal agreement with security for both parties
- Structured to allow parties to share outputs not profits and enables each party to calculate his own tax liability thereafter
- An agreement which can run for 1 year or more
- Fully compliant with EU/DAFF Schemes (inc. REPS)
- Approved by Revenue and DAFF for Cross Compliance rules
- A new land access option to help acquire scale and reduce costs

APPENDIX

Partnership Act 1890

In the Partnership Act 1890 Section 1(1) defines a partnership as “Partnership is the relation which subsists between persons carrying on a business in common with a view of profit”. Section 2(3) of the Partnership Act 1890 states: “The receipt by a person of a share of the profits of a business is *prima facie* evidence that he is a partner in the business, but the receipt of such a share, or of a payment contingent on or varying with the profits of a business, does not of itself make him a partner in the business”.