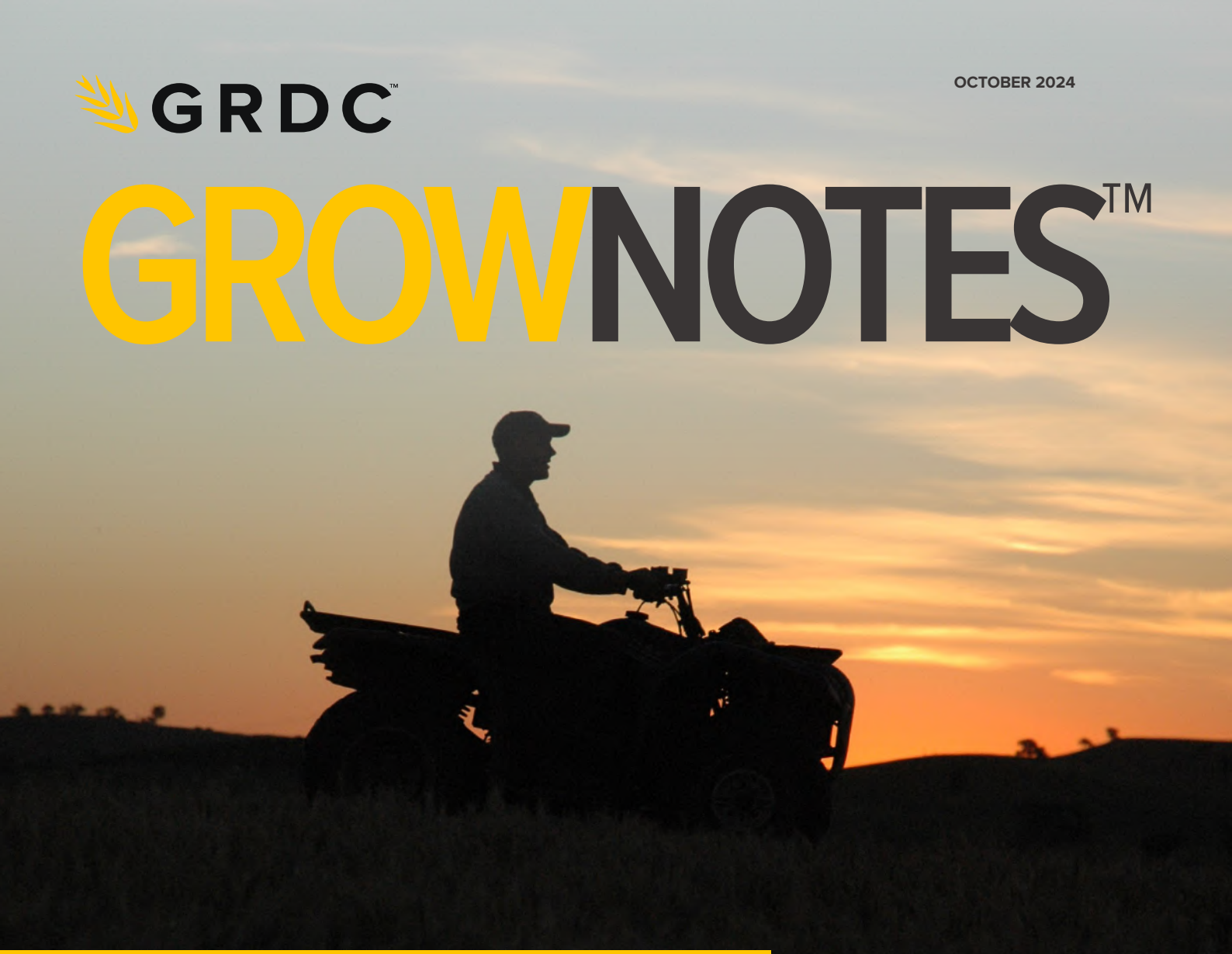
GRDC

OCTOBER 2024

GROWNOTES™



FARM BUSINESS MODELS

GRDC
GRAINS RESEARCH & DEVELOPMENT CORPORATION

Title:
Farm Business Models

ISBN: 978-1-921779-46-6 (online only)

Published:
First edition published November 2017
Second edition published October 2024

Editor: Matt McCarthy, ORM

GRDC contact details:
PO Box 5367
KINGSTON ACT 2604
02 6166 4500
comms@grdc.com.au
grdc.com.au

Design and production:
Coretext, coretext.com.au

COVER PHOTO: Kellie Penfold

Contents

Foreword

Welcome to the updated GRDC *GrowNotes*™ 'Farm Business Models'. This publication was first published in 2017 to provide valuable information on relevant and comprehensive farm business management models to growers, their business partners and farm advisers. It has now been updated to reflect current best practice and new knowledge.

Under the GRDC Research, Development and Extension Plan 2023–28, we are investing in RD&E to create enduring profitability for Australian grain growers. Four pillars drive our investments: 'Harness existing potential', 'Reach new frontiers', 'Grow markets and capture value' and 'Thrive for future generations'. These are supported by four foundational enablers: 'Knowledge transfer and adoption', 'Capacity and ability', 'Data and insights' and 'Innovative partnerships'.

This updated *GrowNotes*™ 'Farm Business Models' is part of our commitment to 'Thrive for future generations', which seeks to ensure Australia's grains industry remains a global leader in sustainability, for people, the planet and our long-term ability to farm.

It aims to help those at the helm of grain growing businesses with knowledge and information on farm business models and structures that can improve profitability, support succession, guide the management of assets and resources, and support financial management and access to capital. GRDC recognises that building farm business management skills and capacity supports the adoption of new and best practices on-farm as well as the embracing of innovative advances in technology.

This publication has been developed to complement other GRDC RD&E investments that are designed to grow farm business management skills, including GRDC's Farm Business Update series. These are online and in-person events that engage with growers and their advisers about farm business challenges and opportunities and bring together experts to discuss new and emerging best practices.

GrowNotes™ 'Farm Business Models' brings together the expertise of respected industry experts, farm financial advisers, researchers and growers to ensure information is relevant, up to date and presented in a practical and engaging format.

I hope you find this a valuable resource for your farming business.

Sincerely,

Nigel Hart
Managing director
Grains Research and Development Corporation

Acknowledgements

The project manager for and major contributor to this GrowNotes was Andrew Rice (ORM Pty Ltd).

ORM was assisted in the development of the publication by a steering committee comprising growers and advisers (Table 1). A subgroup of expert contributors provided detailed input and feedback through the drafting, review and layout stages. ORM would especially like to thank expert contributors Cameron Weeks, David Heinjus and Phil O'Callaghan.

This publication was revised in 2024 by ORM Pty Ltd.

Maureen Cribb (manager Integrated Publications, GRDC) has provided invaluable guidance and ensured that the GrowNote is focused on meeting the needs of grain growers.

In addition, the case study videos, produced by Anvil Media, would not have been possible without insights from growers and their advisers about their experiences with various farm business models (Table 2).

TABLE 1 Project steering committee and expert contributors.

Name	Position	Business	Location
David Brownhill	grower		Spring Ridge, NSW
Basil Doonan	consultant	Macquarie Franklin	East Devonport, Tasmania
John Francis	consultant	Holmes Sackett	Wagga Wagga, NSW
Simon Fritsch	principal	Agripath	Tamworth, NSW
Rod Glass	vice-chancellor's research fellow	University of Southern Queensland	Toowoomba, Queensland
Brian Gregg	grower		Dysart, Queensland
David Heinjus	managing director and consultant	Rural Directions Pty Ltd	Clare, SA
Bec Lanham	consultant	Collaborative Farming Australia	Wangaratta, Victoria
Phil O'Callaghan	managing director and consultant	ORM Pty Ltd	Bendigo, Victoria
Andrew Rice	agribusiness consultant	ORM Pty Ltd	Parkes, NSW
David Sackett	managing director	Growth Farms Australia	Borambola, NSW
Brendan Tierney	grower		Moora, WA
Simon Venus	corporate lawyer	Piper Alderman	Adelaide SA
Cameron Weeks	director and consultant	Planfarm Pty Ltd	Geraldton, WA
Brian Wibberley	principal and accountant	Wibberleys Chartered Accountants	Port Lincoln, SA

TABLE 2 Case study videos.

Name	Position	Location	Business model
Simon Ballinger	grower	Wolseley, SA	Family farm
Scott Campbell	grower	Keith, SA	Family farm
David Heinjus	managing director and consultant	Clare, SA	Consultant
David Critch	grower	Mullewa, WA	Leasing
Alex and Helen Jobling	grower	Swan Hill, Victoria	Share farming
Phil O'Callaghan	managing director and consultant	Bendigo, Victoria	Share farming
Graham Mattschoss		Yorke Peninsula, SA	Joint venture
Paul Schulz		Sandilands, SA	Joint venture
Brian Wibberley	principal and accountant	Port Lincoln, SA	Joint venture

SECTION 1

Introduction to farm business models

VIDEO

Introduction to Farm Business Models GrowNotes™ – Animation
https://youtu.be/TlS2kgfMJ4w

The family farm business model, where the land is owned and operated by the family, has generally served Australian agriculture well. However, there are situations where internal contribution of the farm's assets and operations will not deliver the best outcome for the business or the people involved.

Modifying the family farm model, or developing an alternative model to include some external contribution of assets and/or operations, can deliver greater flexibility and rewards. It may be as simple as tweaking the traditional family farm model to include contracting, through to developing more complex models such as joint ventures.

The technical aspects of running a farm, including crop and pasture agronomy, livestock husbandry and grazing management, are the key building blocks for a sustainable and profitable farm business. However, farm business management is the critical ingredient for success.

Successful farm businesses have two important components: they are profitable and, perhaps more importantly, they meet the needs of the people who own and operate them. Having the right farm business model in place is the first step to achieving success in both.

Family farms, where most or all farm resources are owned or provided by the family, are the dominant farm business model in Australia[1]. Worldwide, agriculture is the only major production sector still predominantly based on the family business model [2].

Statistics suggest the demographics are now changing. In Australia, there is an increasing number of 'family corporates', or large family farm businesses that operate with a formal board and administrative structure with employed staff. In comparison, 'true corporate' farm businesses are companies with shareholders and a board structure. Although the number of 'family corporate' and 'true corporate' farms is still relatively low, their relative contribution to agricultural production is significant[3].

IN FOCUS

Farm business model versus business structure

A farm business model is commonly mistaken to mean 'business structure', or the combination of legal entities for business operation and asset ownership, such as a partnership, trust or company.

While legal entities are important, they are only part of the puzzle and may not take into consideration the foundations for a successful farm business. The business entity is best addressed in the later stages of setting up or restructuring a farm business model, matching the entity to the needs of the business and people. Section 1.1 provides links to additional information on farm business structures.

What is a farm business model?

A farm business model involves arrangements for:

- business ownership and access to **resources**;
- business **management**; and
- sources of **capital** for the business.

Examples of farm business models include leasing, share farming, family farms and joint ventures.

There are many reasons why a grower or 'farm business operator' may consider changing their farm business model. The most common drivers for change include:

- **increased profitability** by improving cost structures and access to resources;
- greater **risk management** through sharing risk with other parties;
- facilitation of **business succession**; and
- increased **access to capital** for growth and operation, reducing the reliance on debt funding.

These drivers are explored further in Section 2.1.

While adopting an appropriate farm business model can help address these drivers, business success also depends on the ability to manage and operate the business well. Traditionally, family farms owned all assets and provided all or most of the resources for operating the business, including land, water, labour, management and working capital. Alternative farm business models provide an opportunity to vary this model to include the contribution of resources from:

- other farm business operators and service providers such as contractors; and
- investors, including landowners not operating their own farm businesses or passive investors offering capital for business operation and growth.

It is essential that the perspectives and needs of all farm business operators and investors are considered when developing farm business models. Models can be customised and multiple models may be included in a business at any one time.

This GrowNote aims to assist growers in assessing their current business model, including their:

- **personal and business circumstances** (Section 2); and
- **farm resources** (Section 3).

It then guides them through:

- **alternative business models** (Section 4)

to assess those that better suit their needs, based on the key considerations of:

- **people**;
- **finances**; and
- **resources**.

1.1. Useful links and additional information – farm business management

GRDC Farm Business Management resources – www.grdc.com.au/Resources

Krause M (2014), *Farming the Business Manual*, GRDC, Canberra – https://grdc.com.au/Resources/Publications/2015/01/Farming-the-Business-Manual

Business Structures Explained, GRDC – https://grdc.com.au/BusinessStructuresExplained

Farm generational transfer – processes and structures, Stephen Park (Pacer Legal) – https://grdc.com.au/resources-and-publications/grdc-update-papers/tab-content/grdc-update-papers/2018/03/farm-generational-transfer-processes-and-structures

Videos
www.youtube.com/playlist?list=PL2PndQdkNRHEJ9OAMJOxlCn53Yh64lOhs

SECTION 2

Assessing your current farm business model

Alternative farm business models cannot be selected 'off the shelf'. They need to be developed to suit specific personal and business needs, focusing on people, finances and resources.

The following steps can be used to better understand your personal and business situation, identifying where changes are required that may be accommodated by an alternative farm business model.

- Step 1 – 2.1. Step 1 – Why change the current business model?
- Step 2 – 2.2. Step 2 – What do the key people in your farm business need?
- Step 3 – 2.3. Step 3 – What stage of the business cycle are you in?
- Step 4 – 2.4. Step 4 – What is your financial position?
- Step 5 – 2.5. Step 5 – What farm resources do you have available?

Farm business management is based on decision-making, choosing a path for your business that has acceptable rewards, both financial and non-financial, for acceptable effort with an acceptable level of risk [4]**.** What is 'acceptable' will vary from business to business and person to person. It is essential that farm decision-making includes all key people in the farm business.

2.1. Step 1 – Why change the current business model?

For existing farm businesses, it is important to understand what is driving the need to explore other business models. For new businesses, what are the drivers for establishing a business? Are you looking for:

- increased profitability?
- greater risk management?
- support for business succession?
- increased access to capital?

These drivers, explored in detail below, are the most common reasons for seeking an alternative business model and will help you develop the most suitable model for your situation, or even help you assess if a change is warranted.

2.1.1. Improved profitability

Profitability is underpinned by productivity, managing costs and access to sufficient resources. Alternative farm business models offer an opportunity to improve profitability through:

- **increased farm business scale**, resulting in stronger bargaining and purchasing power to decrease costs;
- **business relationships with other parties** that can provide access to resources and technology not currently available; and
- **matching resources to the scale of operations**, for greatest economic efficiency.

Better matching resources to scale can benefit businesses of all sizes. For every scale of operations, there is a level of resources that delivers the greatest economic efficiency. It should be noted that farm performance data indicates only a weak relationship between operating scale, measured by gross income, and profitability.

Options to increase the farm business scale of operations include:

- larger area operated, through land purchase, lease, share farming, contracting or joint venture; or
- greater productivity of the current operation by investing in the business.

2.1.2. Risk management

Farm businesses are exposed to a variety of risks, including:

- **production risk** – impact of weather events, such as hail, wind, frost and heat; and pests, weeds and diseases;
- **technology risk** – adoption of new practices;
- **market risk** – variability in commodity prices, market access and product demand;
- **business risk** – payment defaults on farm sales and services; legal responsibilities such as workplace health and safety; changes to suppliers of goods and services;
- **government risk** – legislation changes resulting in additional record-keeping and reporting costs; restrictions on land tenure, management practices and/or land use; and
- **personnel risk** – death, injury, illness and departure of key resources.

Traditional farm business models can leave growers bearing the entire responsibility for managing risks and liabilities, except for those covered by insurance. The scope for managing risk is relatively limited, with options generally based on risk avoidance or mitigation.

Alternative farm business models provide an opportunity for growers to share risk with other parties that are involved in the ownership and operation of the business. Ideally, the risks are shared in a way that is proportional to individual contributions and potential returns.

Farm business models also provide an opportunity to formally separate assets and operations. This is commonly addressed by legal advisers to manage business risk through asset protection. Most of the risk in farm businesses occurs in the operations, so having assets owned by one or more legal entities that are separate to the operation of the farm business can be beneficial.

2.1.3. Supporting business succession

Succession is a complex issue for all businesses and can be particularly so for family farms. Succession involves the transfer of management and ownership of business operations and assets.

Traditionally, succession has been implemented at the point of retirement, although for many growers retirement is delayed until ill health forces the decision. An increasing number of farm businesses are now recognising the importance of early succession planning. Often this is triggered by key personal or farm business events[5] such as:

- marriage;
- birth of a child;
- children finishing school;
- taking on major debt;
- significant financial loss, often as a result of a specific event or drought;
- transfer of business responsibility, often when a child assumes full management responsibility from parents; or
- injury, illness or death of a family member.

Understanding the needs of the key people in the farm business and designing a business model to suit can simplify the succession process. A suitable model can enable growers to exit farming in a manner and timing of their choosing. It can also enable growers to continue their involvement in the business without relying on their physical capacity. Succession in the family farm business model is discussed further in Section 4.1.3.

IN FOCUS

Business structures for succession

An important component of the farm business model in relation to succession is the business structure. The business structure can include one or more legal entities such as sole trader, partnership, company or family trusts.

An appropriate business structure can provide a smooth pathway for the transfer of management and asset ownership in farm business succession. It can also provide asset protection, effective management of income taxation and provisions for off-farm family members[6].

Growers should consult with qualified professional advisers to assess the specific financial, taxation and legal implications of entities for their own personal and business circumstances. Links to general resources can be found in Section 2.6.

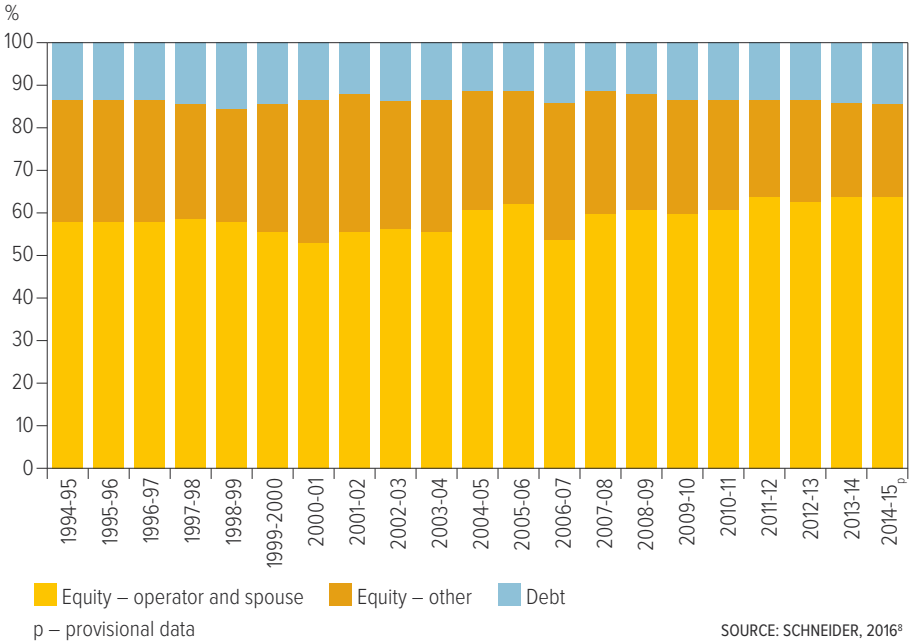
2.1.4. Access to capital

Farm businesses are capital intensive with often high demands for growth, development and working capital.

Most Australian family farms are funded by a combination of equity and debt finance[7] (Figure 1). With sufficient equity, this approach is generally the simplest to establish and manage on an ongoing basis and often provides a cost-effective source of capital.

Recent data shows that 64 per cent of total capital in Australian farm businesses is supplied by internal equity funding through the business operator and their immediate family, with 22 per cent supplied by equity from an external source[8].

Figure 1: Sources of farm business capital for Australian broadacre and dairy farm businesses, 1994-95 to 2014-15.



p – provisional data

SOURCE: SCHNEIDER, 2016[8]

Internal equity is generated by the farm business through appreciation of assets and retained profits. In some situations, farm succession can have a significant impact on internal equity available for capital, with a portion required to fund the retirement of older generations and provide for, or pay out, off-farm family members. The steady increase in land values in recent years has compounded this impact.

Sourcing capital through external equity can be complex to establish and manage and requires a return to the investor. It will therefore generally be more costly than debt finance.

However, the capacity for debt finance to fund capital requirements is limited, given the reliance on land as loan security and gearing ratios, such as the loan-to-value ratio, used by Australian banks. Trade finance is unable to meet the total working capital needs of farm businesses given the current level of debt[7].

Access to capital is one of the primary barriers to farm business expansion and new entrants, particularly where there is insufficient internal equity. With the asset value of an average broadacre farm around $10 million, there are few opportunities using traditional farm business models for young people, outside family succession, and for new entrants to independently own and operate farm businesses[9]. However, opportunities do exist with alternative farm business models where only some of the farm business resources are provided by the owner, therefore reducing capital requirements for business operation. Contracting, share farming or leasing are typical examples. Options to access capital using these models are explored further in Section 4.

2.2. Step 2 – What do the key people in your farm business need?

When developing a farm business model, it is essential to consider the needs of all key people involved.

While the priority will naturally be to focus on people who own and/or manage the business, alternative farm business models involve other parties whose requirements also need to be considered to ensure a successful partnership. Other parties may include:

- investors;
- landowners;
- contractors;
- lessees;
- share farmers;
- employees; and
- advisers.

Alternative farm business models offer the opportunity to better match the business to the needs of the key people involved in the business. The needs will be diverse, but are likely to be based on:

- stage of life;
- aspirations for lifestyle and associated level of involvement in the business; and
- attitude to risk.

These are also important components of business succession planning, which may be one of the drivers behind developing an alternative business model, as addressed in Section 2.1.3.

Stage of life is not purely age dependent, as is often the case with retirement. It can also be defined by significant personal events, such as changing career or starting a family. Irrespective of the timing, these events have an influence on the suitability of different business models for the key people in a farm business.

Aspirations for lifestyle can change with stage of life. Management and operation of a farm business requires significant time and energy commitments. While there is some scope to manage the impact on lifestyle, inevitably a high level of involvement in the farm business will come at some cost to lifestyle.

Attitude to risk is personal and can range from wary to risk seeking; it may change according to stage of life and past experiences. Understanding the risk attitude of key people will help to identify their needs and pathways for working with others in the business. Ultimately, all key people need to be comfortable with the risks involved. Effective risk management is an integral part of running a successful farm business, providing the opportunity to maximise positive business outcomes, avoid or minimise losses and capitalise on opportunities.

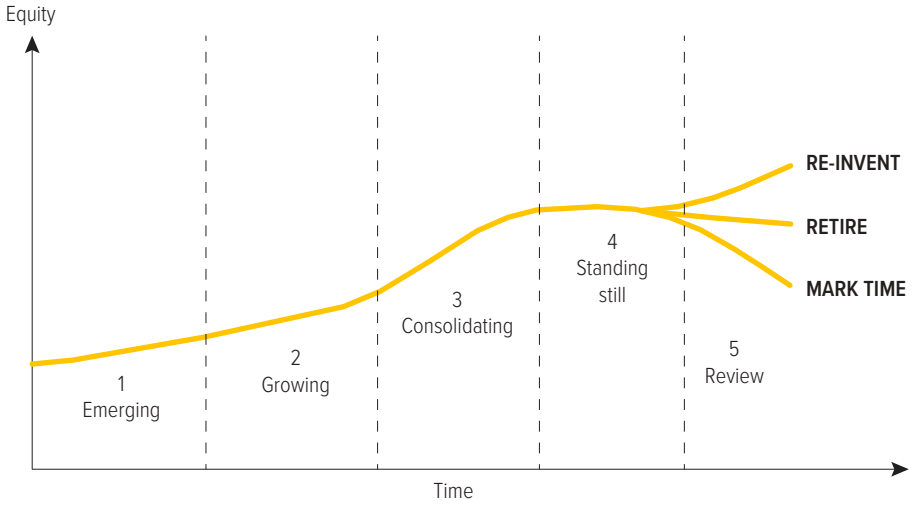
2.3. Step 3 – What stage of the business cycle are you in?

Family farm businesses commonly progress through a business 'life cycle', with identifiable stages and duration that span the working life of a generation[10]. Most often, the primary goal is growing the business to accommodate the next generation.

Business 'life cycle' stages (Figure 2) are commonly linked to business equity and can be typically identified as:

- emerging;
- growing;
- consolidating;
- stable; and
- transitional – the point at which the business reaches a 'crossroads' with the option of:
  - reinventing, through expansion or next generation;
  - retiring or reducing involvement; or
  - winding up.

Figure 2: Stages of business cycle.



SOURCE: CLARK & O'CALLAGHAN (2013)[10]

As the family farm business model has evolved, it is now common to find more than one generation involved in the business at any one time. A 2013 GRDC-funded farm business study of the eastern wheatbelt of Western Australia found that 50 per cent of farm businesses had two generations actively involved in the farming operation[11].

Where overlapping generations occur, the business life cycle is not as easy to track and the link between the stages and business equity is not as strong. However, there can be strong relationships between the stages and scale of the business, measured either as total value of assets, gross income or area operated.

While the business as a whole may not be mapped easily, individuals will identify with key stages in relation to their own involvement in the business. Each stage in the life cycle has implications for appropriate business goals and financial performance targets and benchmarks[12].

MORE INFORMATION

Farming the Business manual

2.4. Step 4 – What is your financial position?

While the needs and aspirations of key people are critical when developing a farm business model, they do not always match the financial capacity of the business. Alternative farm business models may offer pathways to overcome financial constraints, depending on the business's financial position or stage in the business life cycle.

The financial position of the business will influence the ability to:

- access capital; and
- manage fluctuations in financial performance.

Where the financial position of the business is weak, with low equity and/or cash flow, the ability to access capital is limited. Alternative farm business models can:

- reduce capital requirements, accessing capital from other parties for growth, development and operations; and
- share costs and risks.

2.5. Step 5 – What farm resources do you have available?

Assessing farm resources, including assets and operations, is a form of 'stocktake'. The assessment is an effective process for developing a business model that can address capacity issues associated with over or under-utilisation.

Each resource, including land, water, livestock, machinery and labour, should be described in terms of:

- condition;
- capacity;
- suitability to the farm business; and
- improvements or maintenance required.

For example, in a cropping business, machinery is a resource that may be over-utilised, resulting in poor timing of key operations. An alternative model may involve the use of machinery contractors. Alternatively, where existing machinery is under-utilised, excess capacity presents an opportunity to expand by contracting out machinery or accessing additional land through purchasing, leasing or share farming.

The key resources of a farm business are explored in detail in Section 3, including how each resource can be accessed in alternative farm business models and how to value their relative contribution to the business.

2.6. Useful links and additional information – assessing your farm business

Improving profitability

How to make good farm expansion decisions – https://grdc.com.au/Research-and-Development/GRDC-Update-Papers/2015/03/How-to-make-good-farm-expansion-decisions

Farm decision making – https://grdc.com.au/FarmDecisionMaking

Business succession

A Guide to Succession: Sustaining farm families and farms – https://grdc.com.au/GRDC-Guide-Succession-SustainingFamiliesAndFarms

Succession planning fact sheet – https://grdc.com.au/GRDC-FS-SuccessionPlanning

Financial position, assessment of financial performance and resource utilisation

Farming the Business manual – https://grdc.com.au/Resources/Publications/2015/01/Farming-the-Business-Manual

Farm business costs fact sheet – https://grdc.com.au/FBM-FarmBusinessCosts

Machinery investment and costs fact sheet – https://grdc.com.au/FBM-MachineryInvestmentAndCosts

Videos

Farm business models case studies – https://grdc.com.au/farm-business-models-playlist

SECTION 3

Farm resources – how can you access them more effectively?

Farm resources can be broadly categorised into 'assets' and 'operations'. Farm assets include land, water and livestock, while operations encompass management, labour and machinery.

3.1 Separating farm assets and operations

Farm assets and operations are commonly separated in a business structure to protect assets from operational risks (Section 2.1.2).

However, it is also beneficial to separate assets and operations in a farm business model to allow greater flexibility in management and rewarding contributions. The ability to define the relative contributions associated with each farm resource, value them and provide a reward is critical to the success of farm business models.

In the traditional family farm model, farm assets and farming operations, including management and labour, are usually provided solely by the family. The contribution each resource makes to the farm business is typically not specifically or fully valued and rewarded.

In alternative models, farm assets and farming operations are separated so that some can be provided by the business and the balance by other parties, with each party being rewarded for their respective contributions.

Corporate farming is based on the separation of farm business resources, with clear separation of farm asset ownership, business management and reliance on employed labour for farming operations[2].

An increasing number of family farms are evolving towards the corporate model through changes to some of the business resources. Sometimes referred to as 'family corporates', many of these businesses operate with formal board and administrative structures as well as employed staff[1].

Where a farm's assets are provided by different parties within the business model, it is important to link their ownership through a suitable business structure, using legal advice. Where farming operations are provided by different parties, an agreement can be used rather than a formal business structure. Share farming is a common example of an agreement covering the contribution of farming operations including management, labour and machinery.

IN FOCUS

Separating farm business assets and operations

Farm business models that separate assets and operations are more likely to be successful in:

- business risk management (see Section 2.1.2);
- farm succession planning (see Section 2.1.3); and
- increasing the access to capital for the business, including external investors (see Section 2.1.4).

Basic principles of the farm business model

The following principles are critical to the success of farm business models:

- the farm business can be broken down into business **resources**;
- the resources help define the relative **contributions** to the farm business; and
- the contributions to the farm business can be **valued and rewarded**.

Land is the most common example of a resource that is valued and rewarded. Lease payments made under lease agreements are a 'reward' for the contribution of land as a key resource to a farm business.

3.2 Exploring farm resources in detail

Within the categories of assets and operations, farm business resources can be broken down into:

- land;
- irrigation water, where applicable;
- livestock, where applicable;
- management;
- labour and machinery; and
- capital.

In the traditional family farm model, these resources are typically provided internally by the farm owner(s). Although the family farm model has generally served Australian agriculture well, there are situations where accessing certain assets and operations externally will deliver a better outcome for the finances of and key people involved in the farm business.

The following sections explore these resources in relation to farm business models, including how they can be accessed for use in the business and how to value their relative contributions to the business. A summary is provided in Table 3.

TABLE 3 Summary of farm business resources.

Farm business resource	Access options		Rewards for contributions
	Internal	External	
Land	■ Ownership by business owner/operator(s)	■ Lease ■ Share farm ■ Joint venture (various)	■ Lease value – market rates
Irrigation water	■ Ownership by business owner/ operator(s)	■ Temporary trade in allocation ■ Lease	■ Temporary trade value – market rates
Livestock	■ Ownership by business owner/operator(s)	■ Agistment ■ Livestock lease ■ Share farming	■ Agistment rates – market rates ■ Lease value – market rates ■ Share farming – proportional to share of costs
Management	■ Provided by business owner/operator(s)	■ Employees ■ Contractors	■ Full-time – market value for employee of suitable skills and experience ■ Part-time – professional market rates ■ Performance incentives – % share of farm profit
Labour and machinery	■ Provided by business owner/operator(s)	■ Contractors ■ Share farm ■ Machinery syndication	■ Labour – market rates ■ Machinery contract – market rates ■ Machinery syndication – share of profit determined by ownership share of syndicate
Capital	■ Equity provided by business owner/operator(s) – retained earnings.	■ Debt finance through commercial lenders, trade finance, family and friends ■ Equity finance through family and friends, private investors, venture capitalists, stock market, government or 'crowd funding'	■ Debt finance – market rates ■ Equity finance – share of profits based on share of equity

3.2.1. Land

The significant relative value of land and associated infrastructure, compared to other farm resources, means it plays a major role in developing a suitable farm business model.

In a traditional family farm business, the land is owned and operated by the family. However, separating ownership of the land from the farming operations and accessing land through an external party provides an opportunity to reduce capital requirements of the business and/or use the capital elsewhere. This can have benefits for:

- new entrants to farming, who can operate a farm business through leasing or share farming without the capital required to purchase land; and
- existing farm businesses, which can expand their operations through leasing or share farming with little or no additional capital investment other than working capital.

The benefits of accessing land through an external party, including lower capital requirements and reduced financial risk, need to be weighed up against the negatives of not owning land. Land ownership provides a potential source of financial return through growth in land values, as well as business equity and security for capital borrowings.

Farm businesses can access land through:

1. **internal ownership** – where land is owned by the operator, as in a traditional family farm model. Although there may be separate entities for land ownership (for example partnerships or trusts), members of the farm family are connected to the ownership structures and are therefore the common link; and
2. **external ownership** – where land is accessed through leasing, share farming or joint ventures. Joint ventures offer the opportunity for a mixture of internal and external ownership or solely external ownership.

The capital requirements for land are directly related to internal or external ownership. Internal ownership requires capital for land to be provided by the farm business using either internal equity or debt finance. Internal equity is limited by 'self-funding' options such as business revenue or contributions from business members. External ownership enables opportunities for sourcing capital from external parties in return for equity in the land and/or business operations.

Complexities can occur where there is a combination of internal and external ownership of land; for example, in some joint ventures. Land owned in the name of internal and external parties needs to be 'sold' to the remaining party. This sale incurs costs and taxes that should be accounted for in the exit arrangements of a farm business model (discussed in Section 4.5.3).

Rewarding land contributions in a farm business model

Land contributions can be directly equated to an equivalent 'lease value', even though the farm business model may not be based on leasing land. Leasing is the alternative to internal ownership, so it is an appropriate way to value the contribution or opportunity cost; that is, what could have been earned or paid if the land was leased.

Land lease values are determined through one of the following:

- **percentage of the land's market value** – while this method was originally intended to reflect returns from alternative investments, it has since lost that relevance. Cropping land leases once valued at five to eight per cent of the land's market value can now be around two to four per cent, depending on market value. In some circumstances, the market value of the land will include allowances for fencing and livestock water, but exclude structural improvements if they are not available to or utilised by the lessee;
- **fixed rate per unit of production** – an agreed rate per hectare is paid by the lease holder based on actual production (per tonne of grain) and stocking rate (per head) (where livestock are run); or
- **proportion of financial returns** – the lease value is an agreed 'share' of financial returns. The relative profitability of operating the land is commonly determined by calculating the crop and livestock gross margins; that is, gross income less costs directly attributable to the enterprise.

For the purposes of valuing the contribution of land to the business, the percentage of market value is the simplest to calculate and apply. However, without a link to production or financial returns, it has the potential to over or underestimate the value of the land and its contribution to the farm business. Values equivalent to seven to nine per cent of the market value are likely to exceed what could be viewed as a fair return for the relative contributions to the overall business and exposure to risk.

3.2.2. Irrigation water

For irrigation businesses, water can be considered as both an asset and an enterprise input as it can be purchased to meet crop and pasture requirements.

Markets for irrigation water allow the effective trade of permanent water entitlements and seasonal allocations. This enables efficient pricing and transfer of water resources between irrigators.

Irrigation growers have come to rely on water trading as a means of allocating water to its best, and usually highest, value uses. Water trading is an important tool for irrigators in making production, investment and risk management decisions. It is valuable in a variety of seasonal conditions, not just as a reactive response to droughts. Irrigators have used water markets to tailor water entitlement ownership and trading strategies to suit their business objectives and financial situations[13]. In this way, water has become an integral part of their individual farm business models.

Farm businesses can access irrigation water through:

1. **internal ownership** – where water is owned by the operator; and
2. **external ownership** – where water is accessed through the purchase of allocation, or temporary trade, on a seasonal basis to meet irrigated crop and pasture requirements. Alternatively, water can be accessed through leasing entitlements for a term that spans multiple seasons.

Rewarding irrigation water contributions in a farm business model

Water contributions can be valued based on the current water market, using market values for temporary trade if the water is supplied on a seasonal basis, or leasing entitlement values for longer-term supply.

3.2.3. Livestock

Livestock is unique in that it may be an enterprise in its own right or a management tool used in cropping systems for tasks such as complementing herbicides in controlling weeds or to justify a pasture phase as a break in the cropping sequence.

Farm businesses can access livestock through:

1. **internal ownership** where livestock is owned by the operator, typically where livestock is an integral enterprise of the farm business; and
2. **external ownership**, most commonly through agistment, although options are available for livestock share farming or leasing. Agistment allows livestock to be accessed as a management tool in cropping systems, rather than a long-term enterprise.

Rewarding livestock contributions in a farm business model

The appropriate approach to valuing the contribution of livestock to a farm business depends on whether it is an enterprise in its own right or a management tool for use in cropping systems.

For true sheep enterprises owned by the farm business, livestock leasing values could be used as a guide. Indicative values and terms of agreements could be sought from the leasing models used in the dairy industry.

For livestock share farming, the proceeds of progeny and wool sales are commonly shared in the same proportion as the contribution to production costs. Costs can include labour, feed and reduction in value of breeding stock (difference in value between introduction to the breeding herd/flock and the value when culled). Feed costs include supplements, valued at purchase cost or market value if produced on-farm, and grazing crops and pastures, valued at agistment rates based on feed quality and quantity. The livestock owner supplies the breeding stock and replacements.

3.2.4.Management

In the family farm model, the business is generally managed internally by one or more family members, although additional support may be provided by external advisers.

Some farm business models rely on significant external management input, including employment of management personnel or contract managers. In both North America and Europe, professional farm management consultants are commonly engaged to manage farm businesses on behalf of absentee farm business owners.

Farm businesses can be managed through:

1. **internal management** by the owner; and/or
2. **external management** by employees, professional management contractors or a combination of both.

Rewarding management in a farm business model

Farm business management is best valued at the market rate for external managers, either as a permanent employee, where management is a full-time role, or as a professional contractor for part-time management.

3.2.5. Labour and machinery

For the purpose of assessing farm business models, labour and machinery are considered together as they are often provided as one service; for example, through machinery contracting or share farming.

Labour efficiency is often claimed to be higher in the family farm model, on the basis that family labour is motivated to work harder and longer due to the added profit incentive associated with farm ownership[1].

However, there is evidence that high levels of labour efficiency are achievable with other farm business models.

Farm businesses can access labour and machinery through:

1. **internal provision** of labour, with machinery owned by the business as typical of family farms; and
2. **external provision** of labour through employment, contracting or share farming, with machinery accessed through contracting or machinery syndication.

Rewarding labour and machinery contributions in a farm business model

Labour inputs are best valued at the market rate for both internal and external labour, using:

- permanent employee where full-time labour is required;
- casual employee where only part-time labour is required; or
- contractor where specific skills/experience and tools/equipment are required.

Where machinery is syndicated, rewards are generally based on the share of ownership of the syndicate.

3.2.6.Capital

Capital is required by farm businesses for asset ownership, growth, development and ongoing business operations, or working capital. As described in Section 2.1.4, access to capital is one of the primary barriers to farm expansion and new entrants to the industry.

With alternative farm business models, opportunities exist for reducing the capital required by the farm business operator; for example, through contracting, share farming, leasing or equity partnerships.

Farm businesses can access capital using:

1. **Debt** financed through:

- financial institutions such as banks;
- finance companies;
- suppliers, through trade credit;
- customers, through product sales; and
- private loans from family or friends.

2. **Equity** sourced:

- internally through retained earnings; or
- externally, in return for a share of business ownership and profits, through:
  - family or friends;
  - private investors with no existing relationship to the farm business;
  - venture capitalists/other businesses;
  - stock market, through initial public offerings;
  - government, through business grants; and
  - 'crowdfunding'[14,15].

Debt

The amount of debt finance available for capital will be limited by business equity. As total borrowings for a business increase, with no change in asset values, business equity declines and the financing risk is greater. Lenders will typically limit capital finance when equity is in the range of 50 to 70 per cent, requiring historical and forecast trading results to demonstrate sufficient cash flow to service the debt. Most lenders will be reluctant to provide new lending where business equity falls below 50 per cent, although this will depend on individual business circumstances.

It is also important to remember that the use of debt finance involves the business owner assuming all risk for the capital utilised by the business. There are limits to the amount of risk that can be taken on by farm businesses without affecting financial sustainability and personal health and wellbeing.

Equity

The complexities of exchanging equity and future profits for capital means external equity is not commonly sourced by farm businesses, other than through family or friends.

However, private investors are readily accessible and can be sourced through a variety of internet-based service providers for mid-market investments in farm businesses, ranging from $5 million to $100 million (see Section 3.3). Alternatively, 'crowdfunding' uses social media platforms for businesses to market their business and equity offer. There are two distinct crowdfunding models that are based either on donations or an investment with expectation of a return; investing through crowdfunding is a relatively new chapter in the crowdfunding story and is increasing rapidly[15].

At first glance, crowdfunding for capital to invest in agriculture would seem to be a pathway to a practically limitless source of funds. However, the regulations in place around equity crowdfunding limit its applicability for agriculture within Australia to public (unlisted) companies with assets or income of less than $5 million[15].

While both the above options are non-traditional and have some complexities and potential risks, there are examples of farm businesses that have accessed capital using these pathways.

Rewarding capital contributions in a farm business model

Rewarding contributions of debt finance are specific to the financing agreement, usually comprising interest paid and other costs as set out in the agreement.

Equity capital is generally rewarded via entitlements to future farm business profits. The share of profit to an equity partner generally reflects the relative share of equity in the business.

3.2.7. Reflection and summary

One of the most critical times to review the farm business model is when expansion is being considered. Using the farm business resources as a guide, an initial checklist can be run through.

- Land (and water)
  - Is the expansion permanent? Or is there value in having flexibility to scale down after a period?
  - What is the relative return from use of the land (and/or water) in the farm business?
  - What is the long-term outlook for capital growth in land (and/or water) values?
- Livestock
  - Does the farm business have sufficient equity to fund the purchase of the livestock?
- Management, labour and machinery
  - Is there sufficient management, labour and machinery capacity to run the expanded operations?
- Capital
  - Does the farm business have sufficient equity and cash flow to fund the capital requirements for the expansion?

Sticking with a traditional family farm business, all the 'boxes' for the above checklist should be 'ticked'. If not, considering alternative farm business models opens up opportunities for business expansion where it would not be possible under the current farm business model.

SECTION 4

Finding the right farm business model

This section provides a framework for developing a farm business model that best suits the needs of the farming business and the key people involved. This requires a good understanding of:

- **individual personal and business circumstances and needs** (explored in Section 2); and
- **farm resources**, including a stocktake of farm assets and operations (explored in Section 3).

Due to the range of personal and business needs and differing requirements for resources, most farms operate using a mix of business models. For example, family farms now typically operate with some leasing, some share farming and/or some contracting. The level of asset ownership and contribution to farming operations within each model vary significantly depending on the business circumstances.

These variations mean it is not possible to define discrete business models; rather, it is more appropriate to consider model 'types'. Within the model types, the ownership and access arrangements for each farm asset and operation can range from completely internal to completely external, as described in Table 4.

The primary farm business model types are:

- family farming;
- leasing land;
- share farming;
- contracting, including machinery, labour and/or management; and
- joint ventures.

REMINDER

Farm resources (Section 3.2)

Farm resources can be separated into assets and operations. These are typically further broken down into:

- land;
- irrigation water;
- livestock;
- management;
- labour and machinery; and
- capital.

VIDEO

Joint Venture Partnership – Graham Mattschoss, grain grower, SA
https://youtu.be/JLo3QCJ7ueU

SECTION 4
FARM BUSINESS MODELS

TABLE 4 Primary farm business model 'types' – typical ownership and access arrangements for farm resources.

Farm resource	Family farm	Leasing	Share farming	Contracting	Joint venture
Land ownership	50% to 100% internal	100% external	100% external	100% internal or external	100% internal or external
Irrigation water ownership	50% to 100% internal	100% internal or external	100% internal or external	100% internal or external	100% internal or external
Livestock ownership	100% internal	100% internal	100% internal or external	100% internal or external	100% internal or external
Management access	100% internal	80% to 100% internal	80% to 100% internal	100% internal	100% internal or external
Labour and machinery access	75% to 100% internal	80% to 100% internal	80 to 100% internal	25% to 100% internal	100% internal or external
Capital access	100% internal	10% to 30% internal	10% to 30% internal	10% to 30% internal	100% internal

Note: 'internal' is owned or supplied by the farm business operator, 'external' by another party

Assessing farm business models

In the following sections, each of the common farm business models is assessed based on the requirement for an equitable agreement.

An equitable agreement is built on defining and valuing the relative contributions of all farm resources by each party involved in the farm business. This requires the acknowledgement of all:

- **returns** – current and future, including cash and capital appreciation;
- **costs** – including opportunity and overhead costs; and
- **risks**.

Recognising the costs in an agreement needs to account for 'hidden' costs, or opportunity costs that are easily overlooked. In a share farming arrangement, for example, what is the opportunity cost of the share farmer using their machinery to generate income from contracting? What is the opportunity cost of the landowner leasing the land out? Ownership costs, such as machinery depreciation, insurance and rates on land, also need to be accounted for.

The traditional 'going rate' or district practice for income and cost sharing in farm business models should be avoided. Significant changes have occurred in relative commodity values, productivity, input costs and associated risks since many of these going rates or district practices were defined.

Simple methods to analyse and determine equitable agreements to suit individual business circumstances are presented for each farm business model in the following sections.

REMINDER

Basic principles of the farm business model (Section 3.1)

The following principles are critical to the success of farm business models:

- the farm business can be broken down into business **resources**;
- the resources help define the relative **contributions** to the farm business; and
- the contributions to the farm business can be **valued and rewarded**.

4.1. Family farms

In its traditional form, the family farm model is based on all farm business resources being provided internally. For example, land, water and livestock assets are all owned by the family, with management and farming operations, including labour and machinery, supplied by the family members.

While the family farm model is still predominant in Australian agriculture, most family businesses have some variation in the ownership or operation of the farm's resources. Larger family farms commonly have other business models 'nested' within their business, such as additional land accessed under a lease or share-farming agreement and/or use of machinery to provide contract services.

4.1.1. 'Nesting' business models in the family farm

Nesting business models within the family farm is particularly useful in addressing **profitability and risk management** issues. The incorporation of leasing, share farming or machinery contracting allows better matching of scale and resources in the family business, which can reduce costs. Involving additional parties in the farm business helps share risk.

Where a family farm is looking to increase scale, it is important to first ensure the production aspects of the base farm are running well. Operating at a larger scale can easily multiply the losses associated with enterprises that are not performing. For example, the financial effects of a cropping enterprise that is suffering due to poor agronomic management will be multiplied on additional leased or share farming areas, delivering even greater losses to the farm business.

Nesting business models within the family farm can also be useful for meeting **succession planning** obligations, which were discussed in Section 2.1.3. Reducing capital requirements through leasing or share farming can release capital to 'pay out' non-farming family members. Reduced capital requirements can also allow family members who remain on the farm to restructure and operate viably with smaller areas of land under their ownership. The potential implications of succession planning in family farm agreements are discussed in Section 4.1.3.

Nesting business models within the family farm will usually be possible without needing to adjust the entities associated with business ownership and operation. However, professional advice should be sought on any potential legal implications resulting from changes to the farm business model; for example, public liability associated with operations on land that is leased or share farmed. Adjustments to farm insurance policies may be required and the costs associated with these should be considered when structuring agreements.

Although nesting business models within a family farm can bring potential benefits, it can also incur some downsides if not well planned and implemented. **Avoid changing the farm business model just to 'keep up with the Joneses'. Business models are not a 'one size fits all' structure. It can be easy to get swept up in the momentum if it seems everyone else is doing it.** A change to the family farm business model is not always necessary.

4.1.2. Family labour

One of the key claims for family farms is that they are more 'efficient', particularly in terms of labour utilisation. However, industry figures suggest that high levels of labour efficiency are being achieved with other farm business models.

VIDEO

Family Farm Consultant – David Heinjus, Managing Director, Consultant
https://youtu.be/P6ogo6WIB3Q

When assessing the labour requirements for a family farm, consider the potential for off-farm employment. While not applicable in all situations, off-farm employment has the potential to utilise 'surplus' family labour without any requirements for additional capital or risk exposure. Where surplus family labour is used for machinery contracting, it is important to ensure that the family business is not compromised; for example, competing for timeliness of operations that exposes the business to production risk.

4.1.3. Establishing an equitable family farm agreement

Family farm businesses have traditionally operated without formal business structures and agreements. This was often seen as a strength because of increased flexibility in management and business operations.

However, when dealing with multiple family members and generations, the lack of a formal agreement can result in the benefits of flexibility being outweighed by the risks. Without a clear plan and shared understanding of the day-to-day and longer-term strategic business direction, inefficiencies can creep into business operations. The incentives of business ownership can be eroded if family members do not feel valued or do not have recognised roles and rewards within the business.

Improved succession planning has contributed to an increasing level of structured agreements in family businesses, often occurring earlier in business cycles or when a new generation enters the business. In many succession plans, it is now common for the farm assets to be divided equally, in terms of value, between children. While there is strong reasoning for equality in entitlement, the results may not be equitable for family members remaining on the farm. The principles of equality are contributing to the decline in farm numbers and rising farm debt. There are two competing factors at play within succession:

- succession planning tends to lead to smaller farms as a result of dividing up the farm, or farms, with significant debt levels from paying out off-farm family members; and
- increased scale is required for a viable farm business.

For family farms, it is important to establish an equitable agreement within the family business first, before creating agreements with external parties.

Following are some of the key areas that need to be addressed in family farm business agreements (summarised in Table 5).

VIDEO

Family Farm – Simon Ballinger, grain grower, SA
https://youtu.be/N3E0zT7l7kc

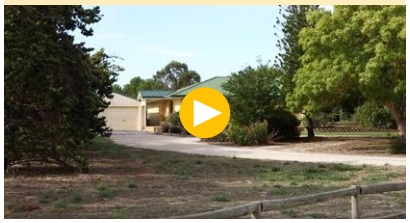


TABLE 5 Developing a family farm business model – summary.

Do	Don't
Consider developing and nesting other business models within the family farm	Make changes to a farm business model that are not linked to a specific purpose
Make changes to the family farm model that provide for the needs of the business and key people involved	Increase the scale of a business that is not already performing well due to production issues
Consider implications of any changes to the model for liability and risk	Make changes to the farm business model without understanding the capacity of current resources
Consider off-farm employment as a valid component of the farm business model	
Plan and budget to assess the impacts of any changes to the farm business model	
Clearly define the roles and responsibilities of all family members; don't make assumptions!	

- **The roles and responsibilities** of all family members working on or in the business need to be defined. This should include off-farm family members who take an active interest in the business and its strategic management.

  In addition to farm tasks, roles and responsibilities also need to account for time, or expectations for hours of work and arrangements for leave. This is one of the most common sources of frustration between generations in a family farm business.

- **Rewards** for contributions of resources to the farm business need to be determined, typically using market values.

  Labour and management in family farm businesses are traditionally rewarded at below market rates, and sometimes go unrewarded. Family farm businesses commonly operate as partnerships, with partners' drawings being the 'reward' for labour and management inputs. Drawings are often minimal and usually only cover living expenses. While this may be equitable for farm businesses with only a single generation and one family, it is difficult with multiple generations and families.

  Recording labour and management inputs to the business and valuing their contribution at market value is the simplest and most equitable arrangement for a family farm business. Without this approach, unpaid rewards to family members lead to increasing growth in their individual equity in the business, and can create problems for succession planning. It can also hide potential inefficiencies and create an unrealistic view of business profitability.

  Reward for contribution to the farm business should not be limited to labour and management. Where family members contribute resources such as land, irrigation water and machinery, the contribution should be rewarded at commercial rates, such as lease or contracting rates.

- **Timeframes**. No item of farm machinery lasts forever and neither does a business agreement. Business agreements need to have a defined period of operation to allow for the changing needs of the business and key people involved.

- **Review**. The agreement should include arrangements for its review, including the 'when' and 'how'.

- **Exit arrangements** need to be defined at the start of an agreement.

4.1.4. Analysis of financial performance – family farms

Analysis of the financial performance of a family farm is best conducted by:

- reviewing historical farm business performance to assess **actual cash flow** over the past five to 10 years;
- assessment of financial position, with a detailed account of assets and liabilities to assess **business equity**; and
- management planning and budgeting for projected performance to assess **projected cash flow**.

4.1.5. Self-assessment – family farm model

After completing an assessment of your own personal and business circumstances as outlined in Section 2, it is then possible to look at alternative business models that may be better suited to your situation. Table 7 provides a self-assessment guide for the family farm business model, focusing on the key considerations of people, finances and resources.

VIDEO

Family Farm – Scott Campbell, grain grower, SA
https://youtu.be/v4UeI0bcbmY

4.1.6. Useful links and additional information – family farms

Wilkinson J and Sykes L (2011), *A guide to succession: sustaining families and farms*. GRDC, Canberra – www.grdc.com.au/GRDC-Guide-Succession-SustainingFamiliesAndFarms

Succession planning, GRDC fact sheet – https://grdc.com.au/GRDC-FS-SuccessionPlanning

Are you a good labour manager? GRDC Farm labour fact sheet – www.grdc.com.au/GRDC-FS-GoodLabourManager

Improving time management and labour efficiency, GRDC Farm Labour fact sheet – https://grdc.com.au/GRDC-FS-FarmLabour-TimeManagement

Machinery investment and costs, GRDC Business Management fact sheet – www.grdc.com.au/FBM-MachineryInvestmentAndCosts

Machinery investment and replacement planning – https://grdc.com.au/resources-and-publications/all-publications/publications/2022/machinery-investment-and-replacement-for-australian-grain-growers

Strategies for staff retention and recruitment – https://grdc.com.au/resources-and-publications/grdc-update-papers/tab-content/grdc-update-papers/2023/06/the-human-agronomy-of-agriculture-identifying-strategies-for-staff-retention-and-recruitment

Videos
https://grdc.com.au/farm-business-models-playlist

VIDEO

Leasing – Daniel Critch, grain grower, WA
https://youtu.be/jxfxGuCIlGs

4.2. Leasing

Leasing, where land ownership is separate to the business operation, is a popular farm business model in its own right. It is also the most common farm business model 'nested' within family farms (Section 4.1.1), being relatively easy to implement without complex agreements.

In recent times, demand for leased land has tended to exceed supply in most regions. Increasingly, this has led to lease values being paid that are above levels where it is possible to operate the lease profitably[16].

While demand for leased land in Australia is high, the supply of land leased for agriculture could be increased with more equitable agreements between the landowner and lessee (farm business operator).

Leasing is a significant form of land tenure in England, Wales, the US and eastern Europe. Studies of leasing worldwide confirm that the key variants of the leasing model are used within Australian agriculture[17], so potential improvements are expected to come primarily through refinement of the current model.

TABLE 7 Self-assessment guide – family farm business model.

Key areas		Key people: family members who own and operate the farming business
People	Stage of life and lifestyle	■ Suits most stages of life, including overlapping generations in the one business. ■ Planning, especially succession planning, is required to meet the needs of multiple generations. ■ Owning and providing all farm resources, including assets and operations, has an impact on lifestyle; reliance on family members reduces availability of both capital and time to spend off-farm.
	Attitude to risk	■ Internal ownership and provision of all farm resources results in the majority of risk being borne by the business and individual family members; may not be compatible with the attitudes to risk for key people in the business. ■ For detailed information on risk profiles see www.grdc.com.au/GRDC-FS-FarmBusinessRiskProfiles
Finances	Stage of business cycle	■ Family farms are best suited to established businesses; relatively high capital requirements for land and working capital may not suit businesses in 'emerging' and 'growing' stages. ■ Unless sold, all family farms will reach 'transition' stage at some point with the need for intergenerational transfer of management and ownership. ■ For detailed information on business cycle stages see Section 2.3.
	Financial position and cash flow	■ Financial position and cash flow largely determine risk capacity. ■ Suits businesses with strong equity to self-fund capital requirements. ■ Low equity can significantly constrain business growth and development and result in high exposure to risk. ■ Suits businesses with strong cash flow to self-fund working capital requirements and service debt. ■ Requires the contributions of family members to be rewarded; unpaid family labour creates an unrealistic view of business profitability.
Farm resources	Land	■ Ownership of land allows the business to capture the benefits of growth in asset value, although returns from growth in land values are not realised until sold. ■ Land represents a significant proportion, usually the majority, of total farm assets.
	Irrigation water	■ Ownership of water allows the business to capture the benefits of growth in asset value. ■ Water can be sold, with allocation offered for sale on temporary trade market, to generate a return from the water without needing to use it within the business.
	Livestock	■ Where livestock is part of farm business operations, ownership allows the business to capture the benefits of growth in its asset value. ■ Risks associated with livestock ownership include stock deaths and declining health.
	Management	■ Inherent incentives with internal provision of management by a family member can increase the commitment to drive business performance. ■ Internal provision of management can also potentially limit the diversity of options and innovation. ■ Conflicts between family members can reduce the effectiveness of internal management. ■ Roles and responsibilities of family members need to be clarified and confirmed. ■ Management contributions of family members need to be acknowledged and rewarded to help avoid inequities that can lead to conflict.
	Labour and machinery	■ Inherent incentives with internal provision of labour can increase the commitment to driving business performance. ■ Conflicts between family members can reduce the effectiveness of internal provision of labour. ■ When combined with off-farm employment, family labour can be very flexible to suit business needs. ■ Labour contributions of family members need to be acknowledged and rewarded to help avoid inequities that can lead to conflict.
	Capital	■ There are limits to the capacity of family farms to self-fund capital through equity and retained earnings.

Key features that distinguish leasing land from other farm business models

- Leases are based on an **agreement between the landowner and lessee**, or farm business operator, where the landowner contributes land for use by the lessee in return for a lease payment.
- The landowner and lessee are **separate business entities**.
- Return to the landowner for contribution of land is through **scheduled, periodic lease payments** made by the lessee.
- The **operating costs and management of the farm business operations are the sole responsibility of the lessee**, accounting for any management requirements or constraints in the lease agreement.
- **The lessee has exclusive rights to the use of the land for the period of the agreement**; only the lessee occupies the land during the lease agreement. This is in contrast to a share farming agreement, where both the share farmer and landowner occupy the land during the agreement.
- **Agreements are covered in some states by Acts of Parliament**; these usually describe the legal obligations of both parties and provide a framework for dispute resolution[21] (see Section 4.2.7).

Leasing versus share farming

Leasing and share-farming business models are closely related, particularly with modifications to the traditional leasing model. A key distinction between the two models is the lease fee.

Lease fees are scheduled, periodic payments that provide the landowner with a return for the contribution of land for use by the lessee (farm business operator). Share farming payments to landowners are generally not scheduled, but are made with the sale of farm produce when the landowner receives a share of the proceeds according to their level of contribution. In a share-farming agreement, the landowner typically contributes a share of input and management costs in addition to land.

4.2.1. Operating solely on leased land

Although leasing is commonly nested within the family farm business model, it is not common for family businesses to operate solely on leased land. This usually only occurs in non-family or corporate farm businesses.

Although operating solely on leased land is viable in a practical sense, there are financial implications. Farm land is the primary form of security for farm business borrowings, including working capital, from banks. When the land is not owned, alternative sources of finance need to be sourced. These often have associated higher costs to reflect the absence of land as security.

Farm businesses operating solely on leased land will have different arrangements for ownership and provision of farm resources compared with the family farm model, where all resources are usually accessed internally. In a leasing model:

- **management** can be supplied internally by the lessee/farm business operator or externally through an employee or management contractor;
- **labour and machinery** are usually supplied internally by the lessee, but can be supplemented externally through employees or machinery contractors; and
- **capital** is supplied both internally and externally:
  - land and associated improvements are supplied externally, which in specialist crop-production farms make up approximately 70 to 80 per cent of total farm capital. External access of capital at 100 per cent would make the farm business a form of joint venture (Section 4.5); and
  - machinery and working capital are generally supplied internally by the lessee.

IN FOCUS

‘Sale and lease back’

There is increasing interest in the use of ‘sale and lease back’ opportunities in Australian agriculture. For a family farm business, the sale of all or part of its land holdings allows capital to be released for alternative uses, including working capital for a new enterprise, expansion or business succession requirements.

The sale and lease back option also provides opportunities for businesses that are in a weak financial position with low equity and constrained by the costs of servicing debt. Selling all or part of the land can provide cash to repay debt and therefore reduce borrowing costs.

Farm businesses have been slower to adopt the sale and lease back option than other industries, mainly due to the security, control and personal satisfaction that comes with land ownership. However, where long-term leases can be secured, the positives of land ownership need to be weighed up against the benefits of reduced capital requirements when operating on leased land.

4.2.2. Developing a leasing model

There is a range of useful and specific information resources available on leasing agricultural land (see Section 4.2.7). Some of the critical considerations when developing a leasing business model are summarised below.

- **Develop a written agreement**. Verbal agreements are often the source of disputes in leasing arrangements. The best approach is to start with an agreement template and use this as the basis of discussions between the lessee/farm business operator and landowner. Once agreement has been reached on the key aspects of the lease, seek professional legal advice to have the lease agreement drawn up. Lease agreement templates and checklists can be found in Section 4.2.7.
- **Conduct a pre-agreement inspection of the land**. Check the condition of the land and improvements and agree on requirements for ongoing maintenance, with details recorded in the lease agreement. The condition of the land, yield potential and required annual costs for nutrients/soil amelioration and weed control should be considered when determining the type of agreement, lease structure and fees. During the inspection, consideration should also be given to the expected condition of land and improvements on hand-back at the end of the agreement. For crop production, it is relevant to consider the residual herbicide activity and any potential effects outside the term of the agreement.
- **Develop a management plan for the operation of the land, including any capital expenditure required**. In addition to crop and pasture rotations, the agreement should include any capital improvements required. Capital improvements are any works or expenses that increase the value of the property and the operating returns over a period longer than the term of the lease. These expenses can be met fully by the landowner, shared by both parties or allowed for in the lease fee. Common capital expenses include:
  - soil ameliorants, such as lime and gypsum;
  - fertiliser applications above annual crop/pasture use;
  - control of existing weed infestations beyond what would be expected in normal crop production;

  - land development, including clearing, drainage or levelling;
  - earthworks, including roads, drainage and erosion control; and
  - fencing.

- **Consider alternative approaches to valuing leases, such as 'participatory' agreements**. The traditional method of valuing leases based on percentage of land value can result in elevated lease fees and affect the viability of the farming operation. 'Participatory' lease agreements are aimed at providing an equitable share of risks and rewards for the operation of the land, based on the relative contribution of farm resources (see Section 4.2.4).
- **Consider longer-term lease agreements**. While leases are commonly for three to five-year terms, some agreements are only for one to two-year terms. Longer terms reduce the risk for the lessee/farm business operator, particularly in traditional lease agreements. This is particularly important in situations where:
  - there are highly variable production environments, such as low-rainfall zone cropping;
  - capital expenses are incurred by the lessee; and
  - the lessee has incurred additional costs to accommodate operations on the leased land, including purchasing livestock, management, labour and/or machinery.
- **Conduct annual reviews** where the lessee and landowner meet to review operation and performance of the agreement.

TABLE 8 Developing a leasing business model – summary.

Do	Don't
Prepare a written agreement.	Use lease values based on land values without considering the implications for profitability of farm business operations.
Conduct a pre-agreement inspection of land. Agree on and record state of land and improvements.	Make the agreement overly complex and time-consuming to administer.
Consider the condition of the land when selecting type of agreement, lease structure and fees.	Make the agreement so simple that it does not meet the needs of both parties, especially with respect to establishing a fair and sustainable lease fee.
Prepare a management plan for the operation of the land.	Overlook reaching agreement on the condition of the land and improvements on hand-back at the end of the agreement. Special consideration should be given to herbicide residues in cropping operations.
Make allowances in the lease agreement for expenditure of a capital nature.	Overlook tax implications of leasing for all parties; seek professional advice on personal and business circumstances.
Consider use of 'participatory lease' models where risk is shared.	Overlook insurance requirements for all parties, including (but not limited to) insurance for assets, public liability and workers' compensation.
Consider longer term agreements, especially where non-participatory agreements are used.	
Conduct annual reviews to review operation and performance of the lease.	

4.2.3. Establishing an equitable lease agreement

For all farm business models, an equitable agreement is developed by considering the relative contributions and perspectives of all parties.

With leasing, there is a clear separation between ownership of the land and the business operation. Typically, the landowner and lessee/farm business operator are unrelated parties. This makes communication about the agreement critical, particularly as the landowner is usually not involved in management of the operations. The only means for valuing contributions is through lease payments.

When establishing a lease agreement, the challenge is to consider and account for the perspectives of both parties. Key considerations for each party include:

1. Farm business operator (lessee)

- Under common agreements, the lease fee is a reward to the landowner for the contribution of land only.
- Other farming resources are supplied by the lessee so the reward for their contribution should be retained by them.
- An equitable lease fee should reflect the relative profitability of operating the land and account for the lessee's contribution of management, labour/machinery and capital. Lease fees calculated as a percentage of land value may result in inflated fees that are not viable.
- Good management practices and demonstration of high productivity can increase the value of land, which can result in increased lease fees.
- The lessee bears all the production risk under traditional lease agreements. The risks can be managed through:
  - the use of participatory lease agreements (Section 4.2.4); and
  - longer lease terms, which provide operators with a longer period of time to generate profits and recoup start-up costs. Leases with five-year terms are reasonable.
- Required capital costs should be identified during negotiations and suitable arrangements made in the lease agreement to accommodate them. This can be managed by:
  - sharing costs, with the lessee paying a proportion that reflects the expected benefits received during the term of the lease. For example, if liming is expected to have a positive effect on production for eight years and the lease agreement is five years, the lessee should pay five-eighths of the lime costs, or 62.5 per cent; and
  - lease terms that match the longest expected period of benefit. Using the lime example above, the appropriate lease term would be eight years.
- Nesting land leasing in an existing farm business model can increase the use of under-utilised resources, such as management, labour/machinery and capital. However, these benefits should be retained by the farm business operator. Their use in farming operations on leased land should be valued at contract rates.
- Lease fees and agreements should account for the scale of the lease area to reflect the impact on profitability and risk within the farm business operation. For example, leasing a small block next door may warrant paying a premium lease fee to reflect potential profitability attributed to the relative ease of management, limited additional costs and likely knowledge of the property. By comparison, leasing a large area some distance away from home base will incur additional costs such as travel, and may also require additional plant and equipment or machinery contractors.
- Lease fees should account for production zones; for example, high-rainfall versus low-rainfall zones for crop production.

- Leasing land can provide a pathway to purchasing the land. Agreements can include arrangements for an option to purchase, providing an opportunity to 'try before you buy'.

2. Landowner

- Under common lease agreements, the landowner contributes the land only, therefore is entitled to a return on the contribution of land only.
- Considering the returns from both the appreciation in land values and lease fee, returns from leasing land should be comparable to returns from other forms of investment to ensure the continued supply of land for long-term lease.
- Continuity of the lease agreement has a value to the landowner. An equitable agreement with a fair lease fee can result in a higher return to the landowner over the longer term.
- Management of the land should ensure that its value is maintained or improved. Participatory lease agreements (see Section 4.2.4), longer lease terms and specific arrangements for capital costs will promote good management practices by the lessee.
- Depending on the circumstances of the landowner, maintaining access to tax concessions as a primary producer may be beneficial, including income averaging and expense deductions, as well as capital gains tax concessions[16]. While professional advice should be sought from a tax specialist, participatory lease agreements are likely to assist in meeting the requirements of the Australian Tax Office (ATO) to maintain tax concessions[18]. ATO rulings on standard lease agreements do not consider landowners to be conducting the business of primary production or the land as being an active asset.

4.2.4. Participatory leases

Under traditional lease agreements, lessees/farm business operators bear all the production risk from year to year, while landowners have a guaranteed return through lease payments. However, over the longer term, some risk is passed to the landowner. Ongoing poor profitability can lead to default on lease payments, disputes and termination of the agreement. Although another lessee may be found, there are costs to the landowner associated with finding, negotiating and securing a new lease.

Although relatively uncommon, participatory leases are a variation on the standard leasing model and provide the opportunity to share risk between the lessee and landowner. In the participatory model, the returns to the landowner are not fixed, but can vary with actual or potential levels of production. Risk sharing arises from sharing the operating costs or profits.

In sharing costs and profits, participatory leases are similar to share-farming agreements. However, they differ in two key respects: participatory leases have regular payments made by the lessee to the landowner, usually in advance; and the landowner does not make a contribution to management.

Participatory leases offer the opportunity to address the needs of both the lessee and landowner by the sharing of risk and accommodating variable returns from the farming of leased land.

There are two common forms of participatory leases:

1. **Profit sharing**, where the relative profitability of the farming operation on the leased area determines the lease payments.

Examples of profit-sharing lease arrangements include[17, 19]:

- **Share of crop gross margin for a 'median year'.**
  - The method for calculating gross margins is set out in the lease agreement. Contract rates are used for machinery operations and other costs as per actuals.

  - Gross margins are calculated for each crop type based on a 'median year' to reflect realistic returns and risks. Median values for crop yields, grain prices and costs should be determined in consultation with both parties.
  - Median gross margins for each crop type are then used to calculate a gross margin for the lease period. The landowner is paid a portion of this gross margin, for example 40 per cent, which needs to be defined in the lease agreement.

- **Base lease plus variable production payment based on actual financial performance.**
  - The landowner is paid a lease payment by the lessee to reflect a base reward for contribution of land.
  - A production payment is also made to the landowner based on an agreed financial target being met or exceeded. Targets are most simply defined as crop gross margins ($/ha). For example, $x bonus for each $/ha above target.
  - The method for calculating gross margins is set out in the lease agreement. Contract rates are used for machinery operations and other costs as per actuals.

2. Production-based, where the lease fee is based on actual grain production (t/ha). This is a simplified version of the second example of profit sharing above.

4.2.5. Analysis of financial performance – leasing

The financial performance of a lease should be assessed over the full term of the agreement to account for fluctuating income and expenses during the crop rotation. An analysis of financial performance can be prepared based on crop gross margins, using realistic figures for expected crop production, inputs and machinery operations. This should be based on a detailed crop-production plan, outlining the crop rotation, expected yields and prices, as well as key inputs such as seed, fertiliser and chemicals. Links to guidelines and templates for the preparation of gross margin budgets are provided in Section 4.2.7.

Although indicative gross margins are available from industry sources (Section 4.2.7), budgets need to be specific to the lease area and proposed management program. Realistic crop yields and grain production should reflect:

- land capability, including soil type and topography;
- local climate, including topographic influences; and
- land use history, which may influence nutrient, pest, weed and disease status.

Developing a management plan that details key inputs through the duration of the lease will help to identify expenses that have a long-term benefit, beyond the term of agreement. Expenditure to address issues such as soil acidity, herbicide-resistant weeds and low nutrient levels can have a significant impact on the profitability of a lease agreement, but can also increase the value of the property. These expense items are capital improvements and should be specifically accounted for in the terms of the agreement, with the costs shared between the lessee and landowner proportional to the relative benefits derived.

A summary of key items in a financial analysis of leasing is shown in Table 9. Most income and expense items can be drawn directly from a standard gross margin budget. The summary includes the following items.

- **Operating costs.** These are the actual costs incurred in the operation of the agreement and the relative sharing between lessee and landowner. Costs for working capital can be sourced from a standard gross margin budget.
- **Operating income.** These are the sources of income under the agreement and the relative sharing between lessee and landowner.

- **Income to individual parties** or 'rewards for contributions'. Operating return from the agreement is calculated by deducting operating costs from operating income.
- **Additional costs to individual parties.** This includes costs that need to be accounted for when analysing the overall profitability of the agreement. For example, the landowner incurs costs such as rates and insurance. The lessee incurs management costs and costs associated with machinery use, such as labour, fuel, repairs and maintenance, as well as depreciation and insurance.

TABLE 9 Summary of income and costs – example of a dryland cropping operation under a leasing farm business model.

Lease analysis – annual summary	Share of total		Comments
	Lessee/farm business operator	Landowner	
Operating costs			
Land	100%		Lease fee paid to landowner
Irrigation water			
Livestock			
Management	100%		
Machinery/labour	100%		
Working capital			
– Seed	100%		
– Fertiliser	100%		
– Crop protection chemicals	100%		
– Contract services – provided by others	100%		Windrowing, aerial spraying
Operating income			
Grain production	100%		
Agistment on crop			
Agistment on stubble			
Income to individual parties			
Share of operating return	100%		As per agreement
Lease payments – land		100%	
Lease payments – water			
Contracting fees - management			
Contracting fees – machinery/labour			
Additional costs to individual parties			
Land – rates, insurance		100%	
Water – licence fees			
Management – labour costs	100%		
Machinery/labour – variable costs	100%		
Machinery/labour – depreciation, insurance	100%		

An example of a complete leasing financial analysis is included in Section 4.6.

4.2.6. Self-assessment – leasing model

After completing an assessment of your own personal and business circumstances as outlined in Section 2, it is then possible to look at alternate business models that may be better suited to your situation. Table 8 provides a self-assessment guide for the 'land leasing' farm business model, focusing on the key considerations of people, finances and resources. As the model can be nested within a family farm business, the self-assessment considers both small-scale (nested) and large-scale (standalone) leasing operations.

4.2.7. Useful links and additional information – leasing

Making profitable leasing decisions – https://grdc.com.au/FBM-LeasingShareFarmingLand

Ashby R and Ashby D (2011), *Successful land leasing in Australia – a guide for farmers and their advisers*, Publication No. 11/052, Rural Industries Research & Development Corporation, Canberra – https://agrifutures.com.au/product/successful-land-leasing-in-australia-a-guide-for-farmers-and-their-advisers/

Preparing a lease agreement, GRDC Business Management fact sheet – https://grdc.com.au/FS-LeasePreparation

Agricultural Tenancies Act 1990 (NSW) is a worthwhile resource when developing a leasing agreement, particularly in relation to the legal responsibilities of each party – www5.austlii.edu.au/au/legis/nsw/consol_act/ata1990233/index.html#longtitle

Gross margin budgets

Farm financial tool: Livestock gross margin budget, GRDC fact sheet – https://grdc.com.au/GRDC-FS-FFT-LivestockGrossMarginBudget

https://grdc.com.au/__data/assets/pdf_file/0032/571496/21112.01-Gross-Margins-Guide-2022_WEB.pdf

Gross margin guides by state

NSW – https://www.dpi.nsw.gov.au/agriculture/budgets

Victoria – https://agriculture.vic.gov.au/farm-management/prepare/tools-and-calculators/hay-vs-grain-calculator

Tasmania – https://nre.tas.gov.au/agriculture/investing-in-irrigation/farm-business-planning-tools

WA – www.agric.wa.gov.au/improvement-tools-gross-margin-analysis

Queensland – https://agmargins.net.au/Reports/Index#

Videos

https://grdc.com.au/farm-business-models-playlist

TABLE 10 Self-assessment guide – leasing business model.

Key areas		Specific considerations	Key people		
			Lessee in small-scale agreement	Lessee in large-scale agreement	Landowner
			Generally suited to:	Generally suited to:	Generally suited to:
People	Stage of life and lifestyle	■ Successful land leasing requires a professional approach by both parties, particularly the lessee; although less time consuming than share farming, commitment to record keeping and communication is required. ■ Irrespective of scale, finding, negotiating and operating lease agreements requires time and commitment to communications. ■ For lessees with a passion for livestock, livestock enterprises are more easily accommodated in land leasing than share farming.	While time requirements are modest, business managers need to have available time to set up and manage agreement.	People with very good communication skills and time to commit where the business operates on multiple leased areas.	Landowners with a financial and personal interest in agriculture but not wanting to be involved in management and operation; and retiring growers or investors looking to invest in agriculture through direct land ownership.
	Attitude to risk	■ Production risk is borne by the lessee with traditional lease agreements; risks for landowner are confined primarily to default on lease payments and failure of lessee to maintain land and improvements. ■ Although 'participatory' lease agreements enable sharing of production risk between lessee and landowner, the nature of lease agreements means the lessee takes on majority of financial risk. ■ Greater flexibility for lessee in managing longer-term risk; under-performing lease land can be removed from business much more readily than if land is owned. ■ For detailed information on risk profiles see www.grdc.com.au/GRDC-FS-FarmBusinessRiskProfiles	Risk exposure is low to moderate; suits a range of attitudes to risk.	Without land ownership the business has lower financial buffering for poor performance. Suits farm business operators who are 'daring', understanding that higher risk can lead to higher returns.	Traditional lease agreements present relatively low risk; suit 'wary' or risk-averse landowners.
Finances	Stage of business cycle	■ Irrespective of stage of business cycle, lessees require surplus farm resources, including management, labour/machinery and working capital. This provides opportunity to reduce marginal costs of production by spreading overhead costs over a larger area. ■ Leasing can be used as a tool in business succession, providing a pathway to business and asset ownership. Land can be leased to next generation, requiring less capital in the early stages of business, and providing returns to the older generation. ■ For detailed information on business cycle stages see Section 2.3.	Suits established businesses due to cash flow and working capital requirements.	Suits growing businesses due to the relatively low capital requirements without land ownership. Can be challenging to fund working capital requirements without land as security.	*Suits landowners in a 'stable' or 'transition' stage; also retiring or retired growers who want to maintain ownership of land as investment. Can be used as part of a succession plan.

	Financial position and cash flow	■ Financial position and cash flow largely determine risk capacity.
		■ Lessee:
		  ■ financial position determines the accessibility of working capital to support expanded operations on lease area and financial buffering to cover losses in poor years; and
		  ■ cash flow is required to service debt for working capital.
			Financial requirements can be more easily accommodated through small-scale leasing, but additional risk to business needs to be managed.	Requires very strong cash flow and sound financial position; lessee provides all working capital under traditional agreements and takes on all production risk. 'Sale and lease back' arrangements can help manage this.	Requires landowners with a sound financial position and low cash flow requirements as rates of return from leasing are equivalent to borrowing costs.

CONTINUED PAGE 43

FROM PAGE 42

TABLE 10 Self-assessment guide – leasing business model.

Key areas		Specific considerations	Key people		
			Lessee in small-scale agreement	Lessee in large-scale agreement	Landowner
Finances		■ Landowner: ■ financial position is less critical with low working capital requirements and no production risk; and ■ cash flow received from scheduled fixed lease payments as determined in agreement, usually paid quarterly in advance.			
			Typical situation:	Typical situation:	Typical situation:
Farm resources	Land	■ Increasing use of non-traditional lease agreements where lessee is rewarded for contributions to improving the capital value of land.	Lease areas are located close to main (home) base; usually traditional lease agreements.	Increasing use of non-traditional agreements to reward lessee for improvement to capital value of land.	Landowner benefits from increases in capital value of the land.
	Irrigation water	■ With developments in water markets and scarcity of irrigation water, irrigation water has become a significant farm asset with both production and investment values. ■ Water entitlement is usually held by the landowner.	'Top up' requirements, where quantity is not met by landowner entitlements, can be purchased on temporary trade market.	'Top up' requirements, where quantity is not met by landowner entitlements, can be purchased on temporary trade market.	Landowner with water entitlements benefits from increases in capital value of the water through market movements.
	Livestock	■ Compared with other models, leasing is generally the simplest means of incorporating livestock in farm business operations.	Livestock generally owned solely by lessee.	Livestock generally owned solely by lessee.	Landowner does not own livestock as part of lease agreement. Joint ownership and/or operation of livestock would require a livestock share-farming agreement.
	Management	■ Management is generally the sole responsibility of the lessee. ■ The lessee usually has exclusive rights to use of the land for the period of agreement.	Responsible for management; must have surplus capacity or ability to source management to meet demands of expanded operations.	Responsible for management; must have surplus capacity or ability to source management to meet demands of expanded operations.	Landowner not involved in management of land during term of lease.
	Labour and machinery	■ Labour and machinery are generally supplied solely by the lessee. ■ Lease agreements can make allowances for specific machinery items to be provided by the landowner, with costs incorporated in the lease fee. This may arise if the landowner was previously a farm business operator.	Supply all labour and machinery; must have surplus capacity or ability to source additional capacity to meet demands of expanded operations.	Supply all labour and machinery; must have surplus capacity or ability to source additional capacity to meet demands of expanded operations.	Landowner not involved in operation of land during term of lease.
	Capital	■ Under traditional lease agreements, working capital for farm business operations is supplied by the lessee.	Supply all working capital for operations; must have surplus capacity or ability to source additional capacity to meet demands of expanded operations.	Supply all working capital for operations; must have surplus capacity or ability to source additional capacity to meet demands of expanded operations.	Requires working capital only to fund direct costs associated with land ownership, including rates and insurances.

*Specialist advice should be sought on impacts of ATO rulings on primary production status and active assets (for capital gains tax)

4.3. Share farming

Share farming was once the most common alternative farm business model, both as a standalone model and as a model nested within family farms. Although leasing is now the most common model nested in a family farm business (see Section 4.1.1), share farming remains a key farm business model in its own right, both in Australia and around the world. Similar to leasing, share farming involves a separation of land ownership from the operation of the business.

Share farming is relatively common in the dairy industry within Australia and New Zealand, particularly as a pathway for new entrants. Although this has also been the case in the grains industry, anecdotally its use has declined, with new entrants tending to favour business models built on land ownership.

Share-farming agreements were once relatively simple, based on income sharing ratios of, for example, 60:40 or 80:20 between the share farmer and landowner, with varying arrangements for sharing costs. However, higher costs and associated risks means share-farming agreements now have to include more complex mechanisms to calculate the respective shares of income.

Share-farming agreements are more complex to establish and operate than land leasing, therefore they require a higher level of communication and trust between both parties.

VIDEO

Share Farm Consultant – Phil O'Callaghan, ORM, Vic
https://youtu.be/yG9vHUT3ZoE

Key features that distinguish share farming from other farm business models

- Share farming is based on an **agreement between the landowner and farm business operator, or share farmer**, where the landowner contributes land for use by the share farmer.
- The landowner and share farmer are **separate business entities**.
- **The operating costs and management of the farm business are shared between the landowner and share farmer**. Where management was once considered the sole responsibility of the share farmer, it is now more common for the share farmer and landowner to consult on key management decisions.
- The agreement includes **pre-defined arrangements for sharing crop and/or livestock input costs**, ranging from zero to 100 per cent.
- **Labour and machinery are typically supplied by the share farmer**, with the agreement recognising the value of these inputs in determining the share of income.
- **The landowner receives a share of income from crop or livestock production**. The share is based on contribution of the land and relative share of total costs, including cash and, in some agreements, opportunity costs.
- Unlike leasing, **returns to the landowner are not scheduled payments or pre-determined amounts**, rather they occur when produce is sold and vary depending on production levels and prices.
- The share farmer does not generally have exclusive rights to use of the land for the period of the agreement. **Both the share farmer and landowner occupy the land during the agreement**. For cropping land, the landowner may use the fallow periods between crops for grazing livestock, unless specifically excluded within the terms of the agreement.
- **Agreements are covered in some states by Acts of Parliament**; these usually describe the legal obligations of both parties and provide a framework for dispute resolution[20] (see Section 4.3.7).

4.3.1. Operating solely on share-farmed land

Farm businesses that operate solely on share-farmed land will have different arrangements for ownership and provision of farm resources compared with the family farm model, where all resources are usually accessed internally. The share-farm model usually acts as follows.

- **Management** is primarily supplied internally by the share farmer, often with some external input from the landowner. Although there is an option to supplement internal management with employed or contract management, this is relatively uncommon in share-farming agreements and creates additional complexity.
- **Labour and machinery** are usually all supplied internally by the share farmer, but may be supplemented externally through employees or machinery contractors; and
- **Capital** is supplied both internally and externally:
  - land and associated improvements are supplied externally, which in specialist crop-production farms makes up approximately 70 to 80 per cent of total farm capital. External access of capital at 100 per cent would make the farm business a form of joint venture (see Section 4.5); and
  - machinery and working capital are generally supplied internally by the share farmer.

4.3.2. Developing a share farming model

There is a range of useful and specific information resources available on share farming (see Section 4.3.7). Some of the critical considerations when developing a share-farming arrangement are detailed below (and summarised in Table 11).

- **Communication and trust** are key elements of successful, long-term share-farm agreements. Generally, good communication will be the key to developing trust. Where either party is reluctant to commit to effective communication, through formal meetings or regular discussions, leasing may be a better option.
- **Develop a written agreement**. Verbal agreements are often the source of dispute in share-farming arrangements. The best approach is to start with an agreement template and use this as the basis of discussions between the share farmer and landowner. Once agreement has been reached on the key aspects of the share-farming arrangement, seek professional legal advice to have the agreement drawn up. Share-farming agreement templates and checklists can be found in Section 4.3.7.
- **Conduct a pre-agreement inspection of the land**. Check the condition of the land and improvements and agree on requirements for ongoing maintenance, usually the responsibility of the landowner, with details recorded in the share-farming agreement. The condition of the land, likely yield potential and required annual costs of nutrients/soil amelioration and weed control should be considered when determining the sharing of costs. This will also assist in determining the appropriate share of production sales. During the inspection, consideration should also be given to the expected condition of land and improvements on hand-back at the end of the agreement. For crop production, it is relevant to consider residual herbicide activity and any potential effects outside the term of the agreement.
- **Develop a management plan for the operation of the land**. A management plan should include crop and pasture rotations and expected input costs and production levels, such as crop yields/quality and stocking rates. A clear understanding of the projected production and profitability of the share-farming operation is required to be able to structure an equitable share-farming agreement.
- **Specify any capital improvements required**. Capital improvements are any works or expenses that increase the value of the property and the operating returns over a period longer than the term of the agreement. These expenses can be met fully by the landowner or shared by both parties in proportion to the expected share of benefits.

VIDEO

Share Farm – Alex Jobling, grain grower, Vic and Phil O'Callaghan, ORM, Consultant
https://youtu.be/CPhLz_scnkE

Common capital expenses include:

- soil ameliorants, such as lime and gypsum;
- fertiliser applications above annual crop/pasture use;
- control of existing weed infestations beyond what would be expected in normal crop production;
- land development, including clearing, drainage or levelling;
- earthworks, including roads, drainage and erosion control; and
- fencing.

- **Consider longer-term agreements**. Share-farming agreements are commonly for three to five-year terms. Longer terms reduce the risk to the share farmer. This is particularly important in situations where:
  - there are highly variable production environments, such as low-rainfall zone cropping;
  - capital expenses are incurred by the share farmer; and
  - the share farmer has incurred additional costs to accommodate the operation, such as extra livestock, management, labour and/or machinery.
- **Conduct annual reviews** where the share farmer and landowner meet to review the operation and performance of the agreement. Due to the contribution of working capital by the landowner, it is particularly important to include them in annual planning. Communication at this level can help reduce issues with payment of input costs during the season.
- **Settle sharing of input costs progressively during the season**. The respective share of input costs should be paid as close as possible to when the costs are incurred, usually each month. Where the share farmer arranges and pays for shared input costs, the landowner should be invoiced for his/her share. For costs specific to the landowner, he/she would ideally be invoiced directly by the supplier. Settling costs throughout the season can avoid a potentially difficult situation where crop failure occurs and costs need to be reimbursed to the share farmer. At the very least, expenses for both parties

TABLE 11 Developing a share-farming agreement – summary.

Do	Don't
Commit to establishing good communication between parties	Make the agreement overly complex and time consuming to administer
Prepare a written agreement	Make the agreement so simple that it does not meet the needs of both parties, especially with respect to sharing capital costs
Conduct a pre-agreement inspection of land. Agree on and record state of land and improvements	Overlook reaching a hand-back agreement on the condition of the land and improvements at the end of the agreement – give special consideration to herbicide residues
Prepare a management plan for the operation of the land, including projected production and profitability to structure an equitable agreement	Forget to include options for crop failure in the agreement: spray out and conserve moisture; cut for hay/silage; graze?
Make allowances in the share-farming agreement for expenditure of a capital nature	Overlook insurance requirements for all parties, including (but not limited to) insurance for assets, public liability and workers' compensation
Consider longer-term agreements	Overlook deciding who is responsible for marketing of produce
Conduct annual reviews on operation and performance of the agreement	
Settle sharing of input costs progressively during the season	

should be reconciled prior to harvest. Consider the use of a professional adviser, engaged jointly by both parties, to help with documentation and negotiations.

4.3.3. Establishing an equitable share-farm agreement

For all farm business models, an equitable agreement is developed by considering the relative contributions and perspectives of all parties.

In both share farming and leasing there is a clear separation between ownership of the land and the business operation although, unlike leasing, the landowner is often involved in management decisions with the share farmer. Typically, the landowner and share farmer are unrelated parties, making communication regarding the agreement critical. The only means for valuing contributions is through the share of production income as defined by the share-farming agreement.

When establishing a share-farming agreement, the challenge is to consider and account for the perspectives of both parties. Key considerations for each party include the following.

1. Farm business operator (share farmer)

- Under an equitable agreement, the share of production income to the share farmer needs to be a fair reward for his/her contribution of management, labour, machinery and working capital, or input costs.
- It is common for the share farmer's management, labour and machinery inputs to be valued inappropriately, or not at all. However, these contributions have an opportunity cost, where they could be otherwise used for contracting to other businesses. They should therefore be valued at applicable contract machinery or management rates.
- Required capital costs should be identified during negotiations and suitable arrangements made in the share-farming agreement to accommodate them. Although sometimes complex, this can be managed through:
  - sharing costs, with the share farmer paying a proportion that reflects the expected benefits received during the term of the agreement. For example, if liming is expected to have a positive effect on production for eight years and the share-farming agreement is five years, the share farmer should pay five-eighths of the lime costs, or 62.5 per cent;
  - share-farming terms that match the longest expected period of benefit. Using the lime example above, the appropriate share-farming term would be eight years.
- Nesting share farming in an existing farm business can increase the use of under-utilised resources, such as management, labour/machinery and capital. However, these benefits should be retained by the share farmer. Their use in farming operations on a share farm should be valued at contract rates.

2. Landowner

- Under an equitable agreement, the share of production income to the landowner needs to be a fair reward for his/her contribution of land, management and working capital, or input costs.
- Reward for the contribution of land needs to be realistic, with lease values likely to be the most appropriate. The lease value should be one that is fair, not at the top end of the market.
- Management of the land should ensure that its value is maintained or improved.
- Depending on the landowner's circumstances, maintaining access to tax concessions as primary producer may be beneficial, including income averaging and expense deductions, as well as capital gains tax[16]. While professional advice should be sought from a tax specialist, share-farming agreements are likely to assist in meeting the requirements of the Australian Tax Office (ATO) to maintain tax concessions[18]. A key consideration to meeting ATO requirements is the contribution to management of the share-farming operation.

4.3.4. Profit sharing agreements

Unlike traditional lease agreements, share farming provides a means of sharing production risk between the landowner and share farmer. With the landowner providing a share of input costs, reflected in their share of production income, they also share the financial loss in a poor season. However, the majority of the production risk is still borne by the share farmer.

A variant of share farming, often referred to as 'profit sharing lease', takes risk sharing to a higher level and potentially offers a more equitable agreement for both parties. Profit-sharing agreements are not common in Australia, but are relatively common in the UK[16,17]. Although the title includes 'lease', profit-sharing agreements do not involve regular, scheduled payments for land. Instead, the land contribution is rewarded through a share of production income, making it a form of share farming.

The key principle with profit-sharing agreements is sharing costs and income in the same proportion, therefore sharing profit equitably and rewarding each party for their contribution of farming resources, as described in the example below. Most importantly, profit-sharing agreements reduce the exposure of the share farmer to production risk and also reduce their capital requirements. For the landowner, profit sharing offers the potential for higher returns.

Example of a profit-sharing agreement, with a 50:50 share of costs and profit in a cropping operation

- **Working capital required for the cropping operation is shared equally between the share farmer and landowner.**
  - This can be achieved most simply by each party depositing equal funds into a joint working bank account, from which all costs are paid. Alternatively, each party pays costs as they occur and invoices the other party for a 50 per cent share of costs. This method can be more complex and difficult to manage.
- **The share farmer is paid contract fees**, as specified in the agreement, for all operations associated with preparing the land, sowing, in-crop operations, harvesting and grain cartage.
  - Contract fees provide a reward to the share farmer for labour and machinery contributions. Where a joint bank account is used, contract fees can be paid using these funds.
- **The landowner is paid a lease payment**, with the value specified in the agreement.
  - Lease fees provide a reward to the landowner for contribution of land. Where a joint bank account is used, lease fees can be paid using these funds.
- **Strategic management of the operations is equally shared between the share farmer and landowner.**
  - Management includes annual review and planning for the operation of the agreement and regular meetings to monitor business performance and approve payment of costs. As equal contributions are made by both parties, there is no need for payments for this strategic management input.
- **Tactical, day-to-day management of operations is supplied by the share farmer, an external adviser or a combination of both.**
  - The agreement needs to specify a value for tactical management provided by the share farmer, for example, using contract management rates.
  - Where a joint bank account is used, management fees can be paid using these funds.
- **Surplus funds after all costs have been met are shared 50:50 between the share farmer and landowner.**
  - Where a joint bank account is used, proceeds from the sale of production are deposited into the account. After all costs have been met, the profit can then be shared equally between the share farmer and landowner.

4.3.5.Analysis of financial performance – share farming

The financial performance of a share-farming agreement should be assessed over the full term of the agreement to account for fluctuating income and expenses during the crop rotation. An analysis of financial performance can be prepared based on crop gross margins, using realistic figures for expected crop production, inputs and machinery operations. This should be based on a detailed crop production plan, outlining the crop rotation, expected yields and prices, as well as key inputs such as seed, fertiliser and chemicals. Links to guidelines and templates for the preparation of gross margin budgets are provide in Section 4.2.7.

Although indicative gross margins are available from state agriculture departments (Section 4.2.7), budgets need to be specific to the share farming area and proposed management program. Realistic crop yields and grain production should reflect:

- land capability, including soil type and topography;
- local climate, including topographic influences; and
- land use history, which may influence nutrient, pest, weed and disease status.

Developing a management plan that details key inputs through the duration of the share-farming agreement will help to identify expenses that have a long-term benefit, beyond the term of agreement. Expenditure to address issues such as soil acidity, herbicide-resistant weeds and low nutrient levels can have a significant impact on the profitability of a share-farming operation, but can also increase the value of the property. These expense items are capital improvements and should be specifically accounted for in the terms of the agreement, with the costs shared between the share farmer and landowner proportional to the relative benefits derived.

TABLE 12 Guideline for allocated share of income and costs between landowner and sharefarmer with two common share arrangements for a dryland cropping operation.

Share-farming analysis – annual summary	Share of total				Comments
	50:50		80:20		
	Sharefarmer	Landowner	Sharefarmer	Landowner	
Operating costs					
Land	0%	100%	0%	100%	
Irrigation water					
Livestock					Livestock operate outside the agreement
Management	90%	10%	90%	10%	
Machinery/labour	100%	0%	100%	0%	Supplied by the sharefarmer
Crop inputs					
– Seed	50%	50%	100%	0%	Who pays crop inputs is key to deciding the share percentages
– Fertiliser	50%	50%	100%	0%	
– Crop protection chemicals	50%	50%	100%	0%	
Contract services – provided by others	100%	0%	100%	0%	
Insurance, crop	50%	50%	80%	20%	
Operating income					
Grain production	50%	50%	80%	20%	
Agistment of livestock					
Additional costs to individual parties					
Land – rates	0%	100%	0%	100%	
Water – licence fees					
Management/agronomist – labour costs	100%	0%	100%	0%	
Machinery/labour – variable costs	100%	0%	100%	0%	
Machinery/labour – depreciation, insurance	100%	0%	100%	0%	

4.3.6. Self-assessment – share-farming model

After completing an assessment of your own personal and business circumstances as outlined in Section 2, it is then possible to look at alternate business models that may be better suited to your situation. Table 13 (see page 52) provides a self-assessment guide for the share-farming business model, focusing on the key considerations of people, finances and resources. As the model can be nested within a family farm business, the self-assessment considers both small-scale (nested) and large-scale (standalone) share-farming operations.

4.3.7. Useful links and additional information – share farming

Preparing a lease agreement, GRDC Business Management fact sheet (many principles apply to share farming) – https://grdc.com.au/FS-LeasePreparation

Leasing and share farming land, GRDC Business Management fact sheet – https://grdc.com.au/FBM-LeasingShareFarmingLand

Agricultural Tenancies Act 1990 (NSW) is a worthwhile resource when developing a share-farming agreement, particularly in relation to the legal responsibilities of each party – www5.austlii.edu.au/au/legis/nsw/consol_act/ata1990233/index.html#longtitle

Videos
https://grdc.com.au/farm-business-models-playlist

4.4. Contracting

The contracting business model typically involves supplying services with surplus capacity, such as machinery, labour or management, to other farm businesses.

The contracting model is commonly nested within family farms. There are relatively few businesses operating purely under a contracting model, although the number is growing. These businesses can be referred to as 'professional contractors', where their operation is based solely on contracting their machinery and labour to other farm businesses.

Conversely, there are relatively few farm businesses that rely solely on contracting to carry out all farming operations, although this is also becoming more common.

Contract agreements are relatively simple to establish and operate. However, good communication between the contractor and the client is essential, particularly where management services are provided.

Machinery contracting is a relatively simple and flexible option to use surplus machinery and labour to generate additional profit. However, careful planning is required to ensure that the demands on resources do not cause undue delays in the timing of key operations in the base farm business.

Management contracting presents an opportunity that is not widely used by farm businesses. Existing farm operators have the opportunity to provide their management expertise on a contract basis to other farm businesses. Similarly, skilled managers can contract their services to farm businesses, without having their own farming operation. While contract management is relatively uncommon in Australia, there is potential for growth.

Contracting, particularly machinery contracting, is commonly used by farm businesses in the US[21] and is known as 'custom farming'. The use of contracting is so common and of such importance to farm business management that annual surveys of 'custom farming' rates are conducted and results published by university extension services. In comparison, there is relatively little information available on contract rates within Australia, which may be an impediment to the growth of agricultural contracting services.

TABLE 13 Self-assessment guide – share-farming business model.

Key areas		Specific considerations	Key people		
			Share farmer in small-scale agreement	Share farmer in large-scale agreement	Landowner
			Generally suited to:	Generally suited to:	Generally suited to:
People	Stage of life and lifestyle	■ Successful share farming requires a professional approach by both parties, particularly the share farmer; can be more time consuming than leasing. ■ Irrespective of scale, finding, negotiating and operating a share-farming agreement requires time and commitment to communications.	While time requirements are modest, business managers need to have available time to set up and manage agreement.	People with very good communication skills and time to commit where the business operates on multiple share-farmed areas.	Landowners wanting modest involvement in farm management and operations; or retiring growers with management skills but not wanting to commit to day-to-day operations.
	Attitude to risk	■ A well-structured share-farming agreement can provide an equitable sharing of risk and reward and will be the preferred model in many situations. ■ Production risk is shared between share farmer and landowner, with the majority borne by the share farmer under traditional agreements; profit-sharing agreements provide a more equitable sharing of risk. ■ Greater flexibility for share farmer in managing longer-term risk; under-performing share-farmed land can be removed from business much more readily than if the land is owned. ■ For detailed information on risk profiles see www.grdc.com.au/GRDC-FS-FarmBusinessRiskProfiles	Risk exposure is low to moderate; suits a range of attitudes to risk.	Risk is lower than leasing with working capital and production risk shared with landowner. Suits farm business operators who are 'neutral' to 'daring', understanding that higher risk can lead to higher returns.	Traditional share-farming agreements present relatively low to moderate risk, but are not suited to 'risk-averse'. Requires a high level of trust in share farmer, including management abilities and honesty.
Finances	Stage of business cycle	■ Share farmer requires surplus farm resources, including management, labour/ machinery and working capital. This provides opportunity for return to skilled management without bearing all the risk, so can suit early stages of business, managed by experienced operators. ■ Landowners can access management expertise and commitment of experienced operators while sharing in rewards of operations. ■ Share farming can be used as a tool in business succession, providing a pathway to business and asset ownership. Land can be share farmed by next generation, requiring less capital in the early stages of business, and providing returns to the older generation. ■ For detailed information on business cycle stages see Section 2.3.	Suits a wide range of business stages as risk and working capital is shared.	Better suited to emerging and growing businesses than leasing due to sharing of risk and working capital, as well as relatively low capital requirements without land ownership; can be challenging to fund working capital requirements without land as security. Less suited to established businesses due to reduced potential profit.	Suits landowners in a 'stable' or 'transition' stage; also experienced growers who want to maintain ownership of land as investment. Can be used as part of a succession plan.

	Financial position and cash flow	■ Financial position and cash flow largely determines risk capacity.
		■ Share farmer:
		  ■ financial position determines level of shared working capital to support expanded operations on share-farming area, and financial buffering to cover losses in poor years; and
		  ■ cash flow is required to service debt for working capital.
		■ Landowner needs to consider implications of working capital requirements and associated risk compared with leasing.
			Financial requirements can be more easily accommodated through small-scale share farming, but additional risk to business needs to be managed.	Requires sound to strong cash flow and financial position; share farmer provides significant working capital under traditional agreements and takes on production risk.	Requires landowner with sound to strong cash-flow and financial position; landowner provides significant working capital under traditional agreements and takes on some production risk.

CONTINUED PAGE 53

FROM PAGE 52

TABLE 13 Self-assessment guide – share-farming business model.

Key areas		Specific considerations	Key people		
			Share farmer in small-scale agreement	Share farmer in large-scale agreement	Landowner
			Typical situation:	Typical situation:	Typical situation:
Farm resources	Land	■ Increasing use of non-traditional share-farming agreements where the share farmer is rewarded for contributions to improving the capital value of land.	Share-farming areas located close to main (home) base; usually traditional share-farming agreements.	Increasing use of profit-sharing agreements to reward share farmer for improvement to capital value of land.	Landowner benefits from increases in capital value of land.
	Irrigation water	■ With developments in water markets and scarcity of irrigation water, irrigation water has become a significant farm asset with both production and investment values. ■ Water entitlement is usually held by the landowner.	'Top up' requirements, where quantity is not met by landowner entitlements, can be purchased on temporary trade market.	'Top up' requirements, where quantity is not met by landowner entitlements, can be purchased on temporary trade market.	Landowner with water entitlements benefits from increases in capital value of the water through market movements.

	Livestock	■ Compared with leasing, it is more complex to incorporate livestock in share-farming agreements.
		■ Livestock can be owned by:
		  ■ both parties, with specific arrangements for entry and exit of agreement; or
		  ■ an individual party, with arrangements for sharing livestock income relative to the contributions to management and operation of the livestock enterprise.
			Livestock owned by share farmer and agistment paid for grazing on share-farm area.	Livestock jointly owned under share-farming agreement.	Livestock jointly owned under share-farming agreement.

	Management	■ Strategic management (annual planning) is generally shared between both parties. ■ Day-to-day management is the primary responsibility of the share farmer.	Responsible for day-to-day management; must have surplus management capacity or ability to source management to meet demands of expanded operations.	Responsible for day-to-day management; must have surplus management capacity or ability to source management to meet demands of expanded operations.	Landowner contributes to strategic management of operations, not day-to-day management.
	Labour and machinery	■ Labour and machinery are generally supplied solely by the share farmer. ■ Share-farming agreements can make allowance for specific machinery items to be provided by the landowner, with reward for contributions accounted for in agreement. This may arise if the landowner was previously a farm business operator.	Supply all labour and machinery; must have surplus capacity or ability to source additional capacity to meet demands of expanded operations	Supply all labour and machinery; must have surplus capacity or ability to source additional capacity to meet demands of expanded operations.	Landowner not involved in operation of land during term of agreement, but contributions can be accommodated.
	Capital	■ Working capital requirements are shared according to terms of share-farming agreement.	Supply significant share of working capital for operations; must have surplus capacity or ability to source additional capacity to meet demands of expanded operations.	Supply significant share of working capital for operations; must have surplus capacity or ability to source additional capacity to meet demands of expanded operations.	Supply significant share of working capital for operations; must have surplus capacity or ability to source additional capacity to meet demands of expanded operations.

Key features that distinguish contracting from other farm business models

- **Contracting is based on an agreement between the contractor and the client**, or other farm business operator, where the contractor provides machinery, labour and/or management for the operation of the client's farm business.
- The contractor and client are **separate business entities**.
- Reward to the contractor for contribution of machinery, labour and/or management is through a **contracting fee**.
- **Costs associated with the contract services are generally the full responsibility of the contractor**, although fuel for machinery contracting is commonly supplied by the client.

4.4.1. Operating solely as a contractor

Contracting is commonly nested within other farm business models, particularly family farms. Most contracting relates to the supply of machinery and labour. Management contracting is relatively uncommon and generally limited to specialist advisory roles such as crop agronomy.

Operating solely as a contractor will have different arrangements for ownership and provision of farm resources compared with the family farm model, where all resources are usually accessed internally. In a contracting model supplying machinery and labour:

- **management** of the contracting business is supplied internally by the contractor;
- **labour and machinery** is usually all supplied internally by the contractor, although some labour may be supplied externally through employees; and
- **capital provision is split** – land is supplied externally by the client, and machinery and associated working capital are supplied internally by the contractor. On average, machinery represents about 13 per cent of total farm asset value.

4.4.2. Developing a contracting model

While contracting agreements are relatively simple when compared with other farm business models, there are some critical elements to consider. These factors are detailed below (and summarised in Table 14).

- **Develop a written agreement**, particularly if businesses are relying solely on contracting as a source of income. Written agreements will assist in negotiations with bankers and financiers, providing evidence of business management capability and future income. Verbal agreements are often the source of dispute in contracting arrangements. Key elements to be included in written contract agreements include:
  - clear identification of the parties involved, including ABN or driver's licence;
  - the term of the agreement, for example one or more seasons;
  - contract fees and basis for charges, such as area or time, measured through GPS guidance or tractor engine hours;
  - items to be supplied by each party, for example fuel and water;
  - expectations regarding timing and timeliness of operations; and
  - specific requirements relating to practices and quality of operations.

A contracting agreement template is provided in Section 4.4.6. Written agreements can be registered under the Personal Property Security Register (www.ppsr.gov.au), which offers the contractor some protection against payment default on contract fees.

- **Consider workplace health and safety (WHS) and insurance obligations for both the contractor and client**. Any potential WHS issues should be discussed when negotiating the contracting agreement. Insurance requirements include, but are not limited to, public liability, assets and workers' compensation.

TABLE 14 Developing a contracting agreement – summary.

Do	Don't
Prepare a written agreement	Overlook WHS and insurance requirements for all parties, including (but not limited to) insurance for assets, public liability and workers' compensation
Define the services to be supplied and associated term	Make assumptions; clear communication is essential
Identify the basis for charges (area or hourly) and items to be supplied by each party	
Consider payment terms and conditions for contract fees	
Discuss expectations regarding timing and timeliness of operations	

4.4.3. Establishing an equitable contracting agreement

Compared with other farm business models, establishing an equitable contracting agreement is relatively straightforward. The contributions of the contractor are limited to the services provided, such as machinery and labour or management.

When establishing a contracting agreement, the challenge is to consider and account for the perspectives of both parties. Key considerations for each party include the following.

1. Farm business operator (contractor)

- The contributions of the contractor are limited to the services provided, such as machinery and labour or management. The value of the contributions should include the direct costs, indirect costs and an allowance for profit. Opportunity costs need to be considered where no direct costs are incurred, for example through the use of family labour. Market rates for labour and machinery or management contracting should be used.
  - Direct costs for management and labour include the value of labour and on-costs such as workers' compensation insurance and superannuation.
  - Direct machinery operation costs include fuel, unless supplied by the client, and repairs and maintenance costs such as parts and labour.
  - Indirect costs include allowances for depreciation, insurance and the opportunity cost of machinery investments.
- An allowance for profit needs to be incorporated into the contract fee, potentially 20 to 30 per cent. In large-scale and/or long-term contracting arrangements, this could be reduced when negotiating contract fees.
- Pricing of contract fees should consider the embedded value in the services provided. For example, in machinery contracting, will there be a degree of management services included? Are specialist skills required for machinery operation and performance of the services?
- Sourcing contracting clients has traditionally been done through local networks. This remains a valuable source, there are now websites and social media platforms to promote contracting services.
- Dry hire of surplus plant and equipment is an option that separates labour from the supply of machinery. This offers flexibility to increase the use of machinery that is only required at certain times of the year.

  - Market rates for machinery contracting can be used as a guide to dry hire rates, deducting an allowance for labour. For example, if the market rate for contract windrowing is $250 per hour plus GST, excluding fuel, and contract labour is valued at $40 per hour, an applicable dry hire rate would be: $250 – $40 = $210 per hour plus GST.

- For large-scale contract agreements and/or agreements with new clients, consider registering the agreement under the Personal Property Security Register (www.ppsr.gov.au). Registering a contracting agreement with PPSR offers the contractor some protection against payment default on contract fees.

2. Client (other farm business operator)

- Timeliness and quality of work are key factors when determining the value of contract services. These need to be specified in the contract agreement.
- There are a growing number of 'professional agricultural contractors' who specialise in contract services instead of having their own farming business. However, 'farmer contractors' still play an important role in meeting client demand with their excess capacity in machinery and labour. Both types of contractors will have competing demands on their time in peak work periods. It is important to determine timeliness requirements for contract work and the capacity of the contractor to meet this.
- Consider options to make the business more attractive to contractors and improve the timeliness and efficiency of operations. For cropping enterprises, this could be achieved by considering the layout of crop areas, for example 'long runs' and 'block farming', as well as improving access to inputs such as chemicals and water for spraying operations.
- Sourcing contractors has traditionally been done through local networks. While this remains a valuable source, there are now websites and social media platforms to locate contracting services.

4.4.4. Analysis of financial performance

While less critical than for other farm business models, the financial performance of a contracting arrangement should be assessed over the term of the contracting agreement, if more than one season. This accounts for the impact of crop rotation on machinery operations or management and allows for the increasing trend towards long-term contracting agreements.

Typically, financial analysis of contracting agreements only considers the perspective of the contractor. However, contracting can be a pathway to other farm business models, such as where the contractor and client consider developing a share-farming or leasing arrangement. In this situation, it would be worth considering the perspectives of both parties when assessing the overall performance of the agreement.

Resources to assist with a detailed analysis of machinery costs and guidance on the process of calculating contracting rates are provided in Section 4.4.6. While contract rates are often set by the 'going' market rate, contractors are encouraged to calculate their own rates as costs will vary between machinery type and condition, including fuel usage, repairs and maintenance, and depreciation. Variations in operating costs can impact on the profitability of the agreement.

A summary of key costs in a financial analysis of contracting is shown in Table 15. The summary includes the following items.

- **Operating costs.** These are the direct costs incurred by the client in the farming operation and can be sourced from a standard gross margin budget.
- **Operating income.** This is the client's income from the farming operation.

- **Income to individual parties** or 'rewards for contributions'. Financial returns to the client are calculated by deducting operating costs from operating income. The contractor's income is sourced through contracting fees for machinery, labour and/or management.
- **Additional costs to individual parties.** These costs are not included in the operating costs but need to be accounted for when analysing the overall profitability of the agreement. For example, a management contractor may incur labour costs such as workers' compensation insurance and superannuation; a machinery contractor incurs costs associated with machinery use, such as labour, fuel, repairs and maintenance, as well as depreciation and insurance.

TABLE 15 Summary of income and costs – example of a dryland cropping operation under a contracting business model (machinery and management).

Contracting analysis – annual summary	Share of total		Comments
	Contractor	Landowner	
Operating costs			
Land			
Irrigation water			
Livestock			
Management		100%	Paid by client to contractor
Machinery/labour		100%	Paid by client to contractor
Working capital			
– seed		100%	Paid by client
– fertiliser		100%	Paid by client
– crop protection chemicals		100%	Paid by client
– contract services – provided by others		100%	Windrowing, aerial spraying, paid by client
Operating income			
Grain production		100%	
Agistment on crop			
Agistment on stubble			
Income to individual parties			
Share of operating return		100%	As per agreement
Lease payments – land			
Lease payments – water			
Contracting fees - management	100%		
Contracting fees – machinery/labour	100%		
Additional costs to individual parties			
Land – rates, insurance		100%	
Water – licence fees			
Management – labour costs	100%		
Machinery/labour – variable costs	100%		
Machinery/labour – depreciation, insurance	100%		

An example of a contracting financial analysis is included in Section 4.6.

TABLE 16 Self-assessment guide – contracting business model.

Key areas		Specific considerations	Key people		
			Contractor in small-scale agreement	Contractor in large-scale agreement	Landowner (client)
			Generally suited to:	Generally suited to:	Generally suited to:
People	Stage of life and lifestyle	■ Successful contract farming requires a professional approach by both parties, particularly the contractor. ■ Finding, negotiating and operating a contract-farming agreement requires time and commitment to communications. ■ Although usually less complex than other business models, time involved with service delivery and ongoing, regular communication with clients can make contracting very demanding during peak periods and requires careful time management/ scheduling.	While time requirements are modest, business managers need to have available time to set up and manage agreement.	Operators with few other farm business commitments.	Landowners can be solely responsible for management and operation of the farm business.
	Attitude to risk	■ Production risk is borne by the landowner. ■ Risks for the contractor are primarily confined to default on client payments. ■ For detailed information on risk profiles see www.grdc.com.au/GRDC-FS-FarmBusinessRiskProfiles	Risk exposure is very low; suits a range of attitudes to risk.	Risk exposure is low; suits a range of attitudes to risk.	Suits 'neutral' to 'daring' risk attitudes, understanding that higher risk can lead to higher returns; all production risk is borne by landowner.
Finances	Stage of business cycle	■ Contractor has low financial risk and ability to help fully utilise farm resources, so suitable for early stages of business development. ■ For detailed information on business cycle stages see Section 2.3.	Suits 'emerging' to 'stable' businesses.	Suits 'growing' to 'stable' businesses.	Suits 'stable' landowners with an accomplished management team to accommodate the day-to-day needs of managing contractors.
	Financial position and cash flow	■ Financial position and cash flow largely determine risk capacity. ■ Contractor has low financial risk, limited to payment default by contracting clients, and low working capital requirements. ■ Majority of working capital requirements are met by landowner, who also bears the production risk.	Accommodates a range of financial and cash-flow positions.	Accommodates a range of financial and cash-flow positions; regular invoicing for contract work is required to maintain liquidity of business.	Suits a sound to strong financial position and cash flow as contract fees will need to be paid during the season before grain proceeds are received.
			Typical situation:	Typical situation:	Typical situation:
Farm resources	Land	■ Land owned solely by client.	No ownership of land where contract services are provided.	No ownership of land where contract services are provided.	Sole ownership of land.
	Irrigation water	■ Water owned solely by client.	No ownership of water.	No ownership of water.	Sole ownership of water.
	Livestock	■ Livestock generally owned solely by client. ■ If joint ownership of livestock, then livestock covered by a livestock share-farming agreement.	No ownership of livestock.	No ownership of livestock.	Sole ownership of livestock.
	Management	■ Management typically supplied solely by client. ■ Contribution of management by contractor can be accommodated and rewarded at market rates.	May contribute to management.	Typically no contribution to management, although contributions can be accommodated.	Sole responsibility for management.

CONTINUED PAGE 59

FROM PAGE 58

TABLE 16 Self-assessment guide – contracting business model.

Key areas		Specific considerations	Key people		
			Contractor in small-scale agreement	Contractor in large-scale agreement	Landowner (client)
			Typical situation:	Typical situation:	Typical situation:
Farm resources	Labour and machinery	■ Labour and machinery can be supplied solely by contractor, or by both contractor and client. ■ Clients may have their own labour and machinery that are used for some operations, with contractors engaged for specific crop or livestock operations.	Labour and machinery solely provided by contractor for crop enterprises.	Labour and machinery solely provided by contractor for crop enterprises.	Landowner relies on contractors for supply of labour and machinery.
	Capital	■ Working capital for operation of the farm enterprise is primarily provided by the client. ■ Contractor normally only supplies working capital to meet costs directly associated with the services, such as labour and machinery repairs and maintenance. Fuel is normally supplied by the client.	Unlikely that returns from contracting will justify the additional capital required to purchase machinery primarily to undertake contracting.	Carefully assess potential returns if additional capital is required to purchase machinery for contracting.	Landowner is responsible for majority of working capital in addition to contracting fees. Although contracting may be the most practical and economic option, cash costs can be higher than operating own equipment.

4.4.5. Self-assessment – contracting model

After completing an assessment of your own personal and business circumstances as outlined in Section 2, it is then possible to look at alternate business models that may be better suited to your situation. Table 16 (see page 60) provides a self-assessment guide for the contracting farm business model, focusing on the key considerations of people, finances and resources. As the model can be nested within a family farm business, the self-assessment considers both small-scale (nested) and large-scale (standalone) contracting operations.

4.4.6. Useful links and additional information – contracting

Example contract farming agreement

Guide to machinery costs and contract rates, NSW DPI Primefact 913 – www.dpi.nsw.gov.au/__data/assets/pdf_file/0011/302699/Guide-to-machinery-costs-and-contract-rates.pdf

Australian Custom Harvesters Inc. (harvest rates) – www.customharvesters.org.au/harvest-rates/suggested-harvest-rates

4.5. Joint ventures (equity partnerships)

VIDEO

Joint Venture Consultant – Brian Wibberley, Consultant
https://youtu.be/dPZ8eLLBh_M

There are many variations of business models that can be described as joint ventures, which in itself can deter farm businesses from considering them as an alternative option. A joint venture can be described as:

> "... a business agreement in which the parties agree to develop, for a finite time, a new entity and new assets by contributing equity. They exercise control over the enterprise and consequently share revenues, expenses and assets." [22]

The joint venture model can be adopted by both corporate farms and family farms. Joint ventures can range from simple models such as machinery syndication (see Section 4.5.7), through to more complex models that present greater opportunities to address the key drivers for alternative business models described in Section 2.1.

When compared with other farm business models, joint ventures provide the greatest opportunity to access alternative sources of capital. They can also provide better access to management expertise through the parties involved.

Compared with other business models, joint ventures are also typically:

- more complex and involve multiple, unrelated parties;
- best established and operated with formal written agreements;
- generally require professional support to design, establish and operate;
- require specialised business structures or entities;
- require all parties to have a close business 'cultural' alignment; and
- involve long-term agreements.

There are relatively few joint ventures operating in Australian agriculture, despite the needs and opportunities for external investment. Debt funding remains the dominant source of external capital in farm businesses.

Highlighting this situation, the domestic superannuation industry invests less than one per cent of its $3 trillion investment pool into the agri-food class[23]. Many fund managers believe that when compared with alternative investments, farm business assets are not easily converted into cash and experience more volatile cash flows.

For the purposes of this document, joint ventures will be discussed in relation to 'equity partnerships'. Equity partnerships generally provide the greatest flexibility and are most likely to suit family farms seeking an alternative business model. Examples of other joint venture models are found in the link below.

4.5.1. Access to capital through joint ventures

Joint ventures provide considerable scope to access other sources of capital as an alternative to debt funding. This is particularly relevant to land purchases, where the scale of the investment and increasing land prices present considerable challenges to farm businesses.

With land representing about 70 to 80 per cent of total farm capital, investing in land is generally profitable but seldom feasible on a cash-flow basis[24]. As a 'growth' asset, land is more suited to equity financing than debt financing, where cash flow is required for servicing debt.

Under the traditional family farm model, the 'land' and 'farming operations' are both owned by the family business, with the overall profitability being a combination of the returns from both. The farming operations primarily deliver a cash return, with little growth in capital value, while the land does not provide a return until it is sold.

Dividing the farming business into two separate businesses, 'land' and 'farming operations', can allow the returns from each to be considered separately and over different timeframes[24] where:

- 'land' returns are measured by changes in asset value over time, with rewards dependent on smart purchase and sale decisions; and
- 'farming operation' returns are dependent on effective, efficient and sustainable use of the farm resources.

The two businesses are a form of joint venture, which would usually be linked in their ownership and operation. The challenge is to determine an equitable return to each party.

4.5.2. Equity partnerships

There are a range of joint-venture models to suit different business drivers. Equity partnerships are one form of joint venture that are usually most suited to family farms, being less complex and generally the most flexible. Note that unlike other business models, equity partnerships are not usually nested within family farms because the capital required to invest is already fully utilised.

Many equity partnerships in Australia and New Zealand are agreements between farm business operators who have ceased their individual family farm businesses to join forces, pooling their resources to form an equity partnership.

Equity partnerships can be described as a joint venture based on an agreement between a few, usually non-related parties such as individuals, partnerships, trusts or companies[25] where:

- the parties contribute capital to invest in a business, therefore becoming equity holders; and
- expertise and other resources are often pooled to set up and operate the business.

Similar to family farm business models, it is critical to have good relationships, clear communication and alignment of goals between all parties in an equity partnership. The success of the joint venture also depends on[25]:

- robust business processes and reporting systems;
- agreed entry and exit processes and strategies for equity holders; and
- agreed processes for dispute resolution.

Key features that distinguish equity partnerships from other farm business models

- Equity partnerships are based on an **agreement between two or more parties, or equity holders**, who contribute equity to a farm business.
- **More than one farm business can be an equity holder.**
- The agreement is based on a relationship between equity holders, which **may involve a separate legal entity, but is not essential.**
- **Farm resources,** such as land, irrigation water, livestock and machinery, may be owned jointly or contributed by individual equity holders, but **are pooled for use by the business irrespective of ownership.**
- **Farm management and labour can be supplied internally by individual equity holders or externally** through employees or contractors.
- The **contributions of equity partners do not need to be equal.** Rewards for individual contributions are based on:
  - a share of profit from the joint venture, determined by their relative share of equity; and
  - the market value of resources owned or supplied by individual equity holders.
- **Risk is shared between all equity holders,** with the level depending on individual equity contributions.

Another similarity to the family farm model involves access to farm resources, where all farm resources are usually owned or supplied internally by the equity partnership.

Where the family and equity partnership business models differ is in the flexibility in ownership/supply of farm resources and sharing of risk. With equity partnerships it is possible for farm resources to be provided wholly internally or externally, or a combination of both. Risk is shared between all equity holders, with the share of risk determined by relative equity contribution. These differences represent significant potential benefits to farm businesses.

4.5.3. Developing an equity partnership model

Unlike other farm business models, there are relatively few information resources available on joint ventures, or more specifically equity partnerships. Establishment and operation of equity partnerships will generally require professional advice and support.

It is sometimes suggested that a farm business needs to be 'investment ready' in order to attract and secure alternative sources of capital. However, there is little understanding of what this actually means in practical terms. Some of the critical considerations when developing an equity partnership model are detailed below (and summarised in Table 17).

- **Find the right people to be involved.** This is critical, as there needs to be close alignment of goals between equity holders. The goals do not need to be the same, but they must be complementary. Alignment of goals requires honest, face-to-face discussion between equity holders and the development of a robust, achievable strategy for creating 'value', consisting of operating profits and growth in capital value.
- **Develop a strategic plan.** This plan should be used to guide the establishment of the equity partnership, ensuring all equity holders are on the same page. It is also a key resource when engaging professional advice and support. The strategy should be reviewed regularly and assessed against individual equity holder goals during the life of the equity partnership. Aspects to be considered in the strategic plan include[25]:

VIDEO

Joint Venture Partnership – Graham Mattschoss, grain grower, SA
https://youtu.be/JLo3QCJ7ueU

- What are the objectives of the equity partnership?
  - What brings the parties together?
  - If all goals are not shared, are they complementary?
  - What farm business resources, in addition to capital, do equity holders bring to the partnership? Can they supply land, irrigation water, livestock, management, labour and machinery for use in the business?
- What is the investment scope and timeframe for the equity partnership?
  - What types of assets, enterprises and production systems will be focused on?
  - Are the timeframes:
    - short term – develop and re-sell for capital gain;
    - medium term – develop, improve production and profitability, expand scale and sell as an established business; or
    - long term – develop, improve production and profitability, expand scale and continue to operate.
- How will the equity partnership be funded?
  - Capital contributions from individual equity holders?
  - Debt funding to supplement capital from equity holders?
  - Agreed arrangements for additional capital contributions from equity holders, if required?
- What is the business structure and processes to deliver the strategy?
  - Consider the legal structure for asset ownership and business operation. The structure needs to allow for unequal equity contributions, ease of entry and exit and business operation.
- Conduct due diligence on investment and operating options or opportunities for the equity partnership, including:
  - asset purchases – land, livestock and machinery;
  - operations – enterprises and production systems;
  - assessing alignment with the strategy; and
  - comparing relative investment and business opportunities.
- Define the role of equity partners in the management and operation of the business.
- Define governance structure and processes.

- **Establish a board of directors or advisory board.** This board should determine and manage strategy, policy and governance for investments and operation of the business. The core roles of the board are to:
  - establish a team for day-to-day management of the business, defining position descriptions and recruiting;
  - establish and review major business policies in areas of human resource management, financial management and reporting, workplace health and safety (WHS) and general risk management;
  - manage returns to equity holders through a dividends distribution policy;
  - manage capital and expenditure; and
  - oversee the management of debt finance.

Ideally, the board would include **independent member(s)** in addition to the equity holders and advisers. These members can provide independent input into the strategic

direction of the business, as well as an independent view when contentious decisions need to be made or there is conflict between equity holders.

- **Consider the options for independent management on a day-to-day basis.** While the scale of operations will determine the practicality of employing a manager or engaging contract management, there may be benefits in having a manager who is not an equity holder. Independent management can remove a potential source of conflict between equity holders, particularly regarding motivations for management decisions, extra rewards derived or responsibility for poor business performance.
- **Develop processes for dispute resolution and the exit of individual equity holders.** Changes to individual and business circumstances can mean an equity holder may want to exit the agreement. Exit strategies need to take into account the time taken to sell and release capital, particularly land, to return to the exiting partner.
- **Develop processes for entry of new equity partners.** Where appropriate, incorporate entry processes into the equity partnership agreement. Entry of new equity partners can provide a pathway for accessing additional capital to fund growth of the business.

VIDEO

Joint Venture – Paul Schulz, grain grower, SA
https://youtu.be/7cottkz-2W0

TABLE 17 Developing an equity partnership model – summary.

Do	Don't
Spend time to find the right people to work with.	Dismiss differences of opinion between equity holders on strategic management; operate on consensus decision-making.
Invest time in honest, face-to-face discussions with potential equity holders.	Overlook the benefits of having independent board members.
Ensure alignment of goals for equity holders.	Underestimate the potential conflict with an individual equity partner being solely responsible for day-to-day management.
Develop a strategic plan for the equity partnership.	Overlook the opportunities associated with taking on new equity partners.
Establish and use a board of directors or advisory board for strategic management of the business and consider the inclusion of independent members.	
Define processes for dispute resolution and exit/entry of individual equity holders.	

4.5.4. Establishing an equitable joint venture agreement

For all farm business models, an equitable agreement is developed by considering the relative contributions and perspectives of all parties. Unlike other models, the establishment of an equitable agreement is integral to equity partnerships and recorded formally through the joint venture agreement.

An equitable agreement under an equity partnership includes the following features.

- Farm business resources, including land, irrigation water, livestock and machinery, may be owned jointly or contributed by individual equity holders, but are pooled for use by the business irrespective of ownership.
- Farm management and labour can be supplied internally by individual equity holders or externally through employees or contractors.
- The contributions of equity partners do not need to be equal. Rewards for individual contributions are based on:
  - a share of profit from the joint venture, determined by the partners' relative share of equity; and
  - the market value of resources owned or supplied by individual equity holders.

4.5.5. Analysis of financial performance – joint ventures

The financial performance of a joint venture should be assessed over the duration of a complete crop rotation to account for fluctuating income and expenses with different crop types. Compared with business models such as leasing and share farming, which tend to operate for terms of two to five years, joint ventures tend to operate for much longer periods, so analysing financial performance over the full term of the joint-venture agreement is likely to be impractical.

An analysis of financial performance can be prepared based on crop gross margins, using realistic figures for expected crop production, inputs and machinery operations. This should be based on a detailed crop production plan, outlining the crop rotation, expected yields and prices, as well as key inputs such as seed, fertiliser and chemicals. Links to guidelines and templates for the preparation of gross margin budgets are provide in Section 4.2.7.

Budgets need to be specific to the joint venture area and proposed management program. Realistic crop yields and grain production should reflect:

- land capability, including soil type and topography;
- local climate, including topographic influences; and
- land use history, which may influence nutrient, pest, weed and disease status.

Developing a management plan that details key inputs through the duration of the joint venture agreement, where possible, will help identify expenses that have a long-term benefit, beyond the term of agreement. Expenditure to address issues such as soil acidity, herbicide-resistant weeds and low nutrient levels can have a significant impact on the profitability of a joint venture operation, but can also increase the value of the property. These expense items are capital improvements and should be specifically accounted for in the terms of the agreement if the land is not owned by the joint venture.

Where the land is owned by the joint venture, the impact of capital improvements on land values is shared by all parties, in accordance with their equity share. However, if the land is owned by one or more of the equity partners and the period of benefits extends beyond the term of the agreement, the costs of capital improvements should be shared between the joint venture and the landowner(s), proportional to the relative benefits derived.

A summary of key items in the financial analysis of a joint venture, specifically an equity partnership, is shown in Table 18. Although equity partnerships can accommodate many variations in how the farming resources are provided, the summary assumes the following contributions:

- land is owned by one of the equity partners – the ‘landowner’;
- management is supplied by another equity partner – the ‘manager’; and
- labour/machinery is supplied by another equity partner – the ‘farm business operator’.

With the exception of land costs, valued at lease rates, most income and expense items can be drawn directly from a standard gross margin budget. Machinery and labour can be valued as opportunity costs, for example using contract rates, which should also allow for depreciation and insurance. Machinery ‘management’ may also be accounted for, allowing an indirect cost for the time associated with planning and monitoring machinery operations.

The analysis assumes a joint working account is established for the agreement, with each party making equal contributions of working capital into the account. All operating expenses are paid from this account.

The summary includes the following items.

- **Operating costs.** These are the actual costs incurred in the operation of the agreement and the relative sharing between equity holders. Costs for working capital can be sourced from a standard gross margin budget. The opportunity

costs, including the lease fee for the land and contracting fees for machinery and management, are shared by all parties. Both working capital and opportunity costs can be paid from the working account to the relevant contributor.

- **Operating income.** These are the sources of income under the agreement and the relative sharing between equity holders.
- **Income to individual parties** or 'rewards for contributions'. Operating return from the agreement is calculated by deducting operating costs from operating income.
- **Additional costs to individual parties** include those that need to be accounted for when analysing the overall profitability of the agreement. For example, the landowner incurs costs such as rates and insurance. The business operator incurs costs associated with machinery use, such as labour, fuel, repairs and maintenance,

TABLE 18 Summary of income and costs – example of a dryland cropping operation under an equity partnership business model.

Equity partnership analysis – annual summary	Share of total			Comments
	Equity partner: farm operator	Equity partner: manager	Equity partner: landowner	
Operating costs				
Land	33%	33%	33%	Paid to landowner as lease value
Irrigation water				
Livestock				
Management	33%	33%	33%	Paid to manager as contracting value
Machinery/labour	33%	33%	33%	Paid to farm operator as contracting value
Working capital				
– seed	33%	33%	33%	Paid directly from working account
– fertiliser	33%	33%	33%	Paid directly from working account
– crop protection chemicals	33%	33%	33%	Paid directly from working account
– contract services – provided by others	33%	33%	33%	Windrowing, aerial spraying; paid directly from working account
Operating income				
Grain production	33%	33%	33%	
Agistment on crop				
Agistment on stubble				
Income to individual parties				
Share of operating return	33%	33%	33%	As per agreement
Lease payments – land			100%	
Lease payments – water				
Contracting fees - management		100%		
Contracting fees – machinery/labour	100%			
Additional costs to individual parties				
Land – rates, insurance			100%	
Water – licence fees				
Management – labour costs		100%		
Machinery/labour – variable costs	100%			
Machinery/labour – depreciation, insurance	100%			

An example of a complete equity partnership financial analysis is included in Section 4.6.

as well as depreciation and insurance. The manager incurs labour costs such as workers' compensation and superannuation.

4.5.6. Self-assessment – equity partnership model

After completing an assessment of your own personal and business circumstances as outlined in Section 2, it is then possible to look at alternate business models that may be better suited to your situation. Table 19 (see page 70) provides a self-assessment guide for the equity partnership farm business model, focusing on the key considerations of people, finances and resources. Although there are several joint-venture models, equity partnerships are suited to the widest range of personal and business circumstances.

4.5.7. Useful links and additional information – joint ventures

Is machinery syndication a good fit for your business? GRDC Business Management fact sheet – https://grdc.com.au/__data/assets/pdf_file/0013/234013/grdc_fs_farmbusinessmodels_hr.pdf.pdf

Videos
https://grdc.com.au/farm-business-models-playlist

4.6. Financial comparisons of farm business models

When comparing the overall performance of alternative farm business models, it is essential to include both financial and non-financial considerations. Considerations that have been discussed in previous sections include the following.

- **What is driving the need to explore other business models?** (Section 2.1)
  - Improved profitability?
  - Risk management?
  - Business succession?
  - Access to capital?
- **What are the personal and business requirements for each party involved?** (Section 2.2 to Section 2.5)

A summary of key financial considerations for each farm business model are presented in Section 4.1 to Section 4.5. These include:

- operating costs;
- operating income;
- income to individual parties, as per agreement; and
- additional costs to individual parties.

For a financial analysis of business models, most costs and income can be sourced directly from crop gross margins using realistic figures for expected crop production (yield and price), crop inputs and machinery operations. These should be based on a detailed crop production plan that outlines the crop rotation, expected yields and prices for each crop type, as well as key inputs such as seed, fertiliser and chemicals. For leasing, share-farming and contracting models, the production plan should cover the full term of the agreement.

To illustrate the relative financial performance of farm business models, an analysis has been prepared using the following example. The actual dollar values will be specific to each farm business; as such, there is no substitute for preparing an analysis based on individual personal and business circumstances.

SECTION 5

Next steps

While good business management remains the key determinant of financial performance within the control of the business operator, alternative farm business models offer the opportunity for the farm business operator to improve profitability, manage risk, facilitate business succession and increase access to capital.

Assessing your own personal and business circumstances is the essential first step when considering alternative farm business models, because a model cannot be selected 'off the shelf'. Models need to be developed to suit personal and business needs, focusing on people, finances and resources.

When comparing the overall performance of alternative farm business models, it is essential to include both financial and non-financial considerations.

Financial analysis of business models can be completed relatively simply using costs and income sourced directly from crop gross margins, using realistic figures for expected crop production (yield and price), crop inputs and machinery operations. These should be based on a detailed crop production plan. The actual dollar values will be specific to each farm business; as such, there is no substitute for preparing an analysis based on individual personal and business circumstances.

Advisers can play an important role in supporting farm business operators and other parties considering alternative models, their relative performance and suitability.

SECTION 6

Endnotes

1 Keogh, M 2015, The family farm is becoming less family, Ag Forum, 9 July 2015, available at www.farminstitute.org.au/ag-forum/the-family-farm-is-becoming-less-family

2 Byerlee, D, Lissita, A & Savanti, P 2012, 'Corporate models of broadacre crop farming: international experience from Argentina and Ukraine', *Farm Policy Journal*, vol. 9, no. 2, pp. 13–25.

3 Nous Group 2015, *Contemporary business strategies and learning models in the agrifood industry*, report for AgriFood Skills Australia, Canberra.

4 Nicholson, C, Long, J, England, D, Long, B, Creelman, Z, Mudge, B & Cornish, D 2015, *Farm decision-making: The interaction of personality, farm business and risk to make more informed decisions*, GRDC project code SFS000028, Grains Research and Development Corporation, Canberra.

5 Barclay, E 2007, *Farm succession and inheritance – comparing Australian and international trends*, Rural Industries Research and Development Corporation, publication no. 07/066.

6 Blackburn, A & Ashby R, 2006, *Financing your farm: a practical guide to financial growth*, 4th edn, Australian Bankers Association and Grain Growers Association.

7 KPMG 2014, *The road to riches: driving investment in Western Australian agriculture*, report to Department of Agriculture and Food, Western Australia.

8 Schneider, K 2016, 'Investing in agriculture – growing our future', 2016 ABARES Outlook Conference, Canberra.

9 ABARES Farm Data Portal https://www.agriculture.gov.au/abares/data/farm-data-portal.

10 Clark, N & O'Callaghan, P 2013, 'Australian farming families are here to stay', *Farm Policy Journal*, Spring, vol. 10, no. 3, pp. 33–43.

11 Kirk, G 2013, 'How to farm profitably in the eastern wheatbelt', Planfarm output from a GRDC project, project code PLN00009, Grains Research & Development Corporation.

12 Beever, G & McCarthy, M 2004, *Business health indicators for professional farmers*, Farm Management 500, Bendigo, Victoria.

13 Guide to Australian water markets https://www.agriculture.gov.au/abares/products/insights/snapshot-of-australian-water-markets#australian-water-markets-why-where-who-and-how.

14 Australian Government (2015), Business information website, available at www.business.gov.au/business-topics/tax-finance-insurance/business-finances/Pages/sources-of-finance.aspx, accessed 14/12/15.

15 Farmers interest in crowd funding https://research-repository.uwa.edu.au/files/140815120/Farmers_interest_in_CF_Authors_accepted_manuscript_20210916.pdf.

16 Ashby, R & Ashby, D 2011, *Successful Land Leasing in Australia – A guide for farmers and their advisers*, publication no. 11/052, Rural Industries Research and Development Corporation, Canberra.

17 https://www.churchilltrust.com.au/project/to-determine-how-australian-farm-succession-and-productivity-can-be-enhanced-through-improved-leasing-practices/

18 Australian Taxation Office, Taxation Determination TD, 95/62, 'Income tax: will the owner (or lessor) of land who allows the land to be used in a sharefarming arrangement be considered to be engaged in a business of primary production as defined by the Income Tax Assessment Act 1936 ('the Act')?', available at http://law.ato.gov.au/atolaw/view.htm?docid=TXD/TD9562/NAT/ATO/00001

18 Some things to consider when share farming and leasing https://www.pinionadvisory.com/wp-content/uploads/2019/08/Share-farming-and-Leasing-Some-things-to-consider.pdf

20 Healey, B 2016, Partner at K&L Gates, personal communication.

21 Plastina, A, Johanns, A & Weets, S 2015, '2015 Iowa Farm Custom Rate Survey' Ag Decision Maker website (www.extension.iastate.edu/agdm), File A3-10, Iowa State University (US), Extension & Outreach.

22 Wikipedia, 'Joint venture', available at https://en.wikipedia.org/wiki/Joint_venture

23 Schlesinger, L 1922, 'Why Super funds aren't investing in agriculture', *Australian Financial Review*.

24 Shadbolt, N & Gardner, J 2003, 'Farm investments: alternative ownership structures that address the liquidity versus profitability conundrum', in *Proceedings of 14th International Farm Management Congress*, Western Australia, Burswood Convention Centre, Perth, 10–15 August 2003.

15 ANZ 2014, 'Equity Partnerships – A look under the bonnet', ANZ Research – *Agri Focus*, April 2014.

List of Tables

List of Figures

List of Videos