Managing Your Timberland Yourself vs. Leasing:

Which Option is Best for You?

Forest landowners always face a variety of alternatives regarding management of their lands. Each landowner tends to be unique in the way he or she chooses to manage. Some manage intensively for maximum production of the timber resource. Others manage for a variety of benefits in addition to timber maximization, such as production of wildlife habitat or aesthetics. Some do not manage at all.

Another option is available for some landowners in certain locations. Some timber companies and institutional investors have, in the past, offered to lease timberland from landowners. Typically, these leases vary from company to company and with each individual situation in terms of length of contract, price paid per acre and other contractual provisions.

The question invariably arises, "Is leasing my forestland a good idea?" The answer to that question depends on a variety of factors. No one answer is correct for everyone. For some people, the constraints placed upon them and their land in a lease arrangement make it an untenable situation. For others, however, the lease is a viable alternative and should be considered. As demand for wood products increases, heavier pressures will be placed on the forest industry to procure wood from private landowners. Thus, it is likely that leases will become more prominent.

This publication examines some hypothetical situations in which comparisons are made between leasing and self-management. The purpose of this examination is not to prescribe any action for the landowner; rather, it is to assist the landowner who is trying to decide whether or not to lease his or her land. These hypothetical scenarios, combined with some general points of consideration, should help guide landowners in their decisions.

Example Self-Management Scenarios

For these scenarios, Winyield® growth and yield computer software was used to simulate results for the self-management options. These assumptions for self-management were made:

- Planted trees per acre = 640.
- Discount Rate or Minimum Acceptable Rate of Return = 10%.
  Site preparation and planting costs were $75 per acre, including a 50% cost share through the State of Louisiana's Forest Productivity Program.
- Property taxes and miscellaneous management costs = $3.50 per year.
- Three different site index scenarios were used (base age 25): site index = 45, site index = 60 and site index = 80.
- Stumpage prices were: pine pulpwood = $20 per cord, pine chip-n-saw = $80 per cord, pine sawtimber = $400 per thousand board feet. Since the analysis assumed self-management of pine plantations, hardwoods were not considered in the analysis. It was assumed that stumpage prices increased in the following manner: pine pulpwood = 1% per year, pine chip-n-saw = 3% per year, pine sawtimber = 2% per year. These price increases are assumed to be over and above inflation.
- For the different scenarios, a final harvest was made in either year 25 or year 30 of the rotation.
- Tax rates: Capital gains tax rate = 18% (for the timber harvest revenues), ordinary income tax rate = 28% (for the hunting lease revenues).

A description of each scenario is in Table 1.

Table 1. Scenario designations and descriptions.

Scenario	Site Index (Base = 25)	Thin #1 (Year)	Thin #2 (Year)	Thin #3 (Year)	Hunting Lease ($ per acre)	Final Harvest (Year)
1	45	17	N/A	N/A	$0.00	25
1A	45	17	N/A	N/A	$7.50	25
2	45	17	25	N/A	$0.00	30
2A	45	17	25	N/A	$7.50	30
3	60	13	20	N/A	$0.00	25
3A	60	13	20	N/A	$7.50	25
4	60	13	20	25	$0.00	30
4A	60	13	20	25	$7.50	30
5	80	13	20	N/A	$0.00	25
5A	80	13	20	N/A	$7.50	25
6	80	13	20	25	$0.00	30
6A	80	13	20	25	$7.50	30

Results of the scenarios are in Table 2.

Table 2. Net present values (NPV's) for each scenario.

Scenario	Net Present Value ($ per acre)
1	$32.64
1A	$91.49
2	$39.92
2A	$101.63
3	$243.00
3A	$302.00
4	$199.59
4A	$261.36
5	$508.11
5A	$566.90
6	$533.00
6A	$595.58

Notice that, in general, NPV's increased with higher site indexes. This stands to reason, since higher quality sites will generate more productive forestland. Also, notice that the scenarios in which a hunting lease income was generated increased the values vs. those scenarios without a hunting lease income. Next we will look at some lease alternatives.

Lease Examples

For the lease analysis, several assumptions were made. They are:

- Tax rate = 28%. Typically, leases are taxed as ordinary income, since the lease revenue is received annually.
- The lease is paid on the first day of the year, every year.
- The lease is for 25 years.
- Lease payments analyzed were $40 per acre per year, $60 per acre per year, $80 per acre per year, $100 per acre per year and $120 per acre per year.

Net present values for the lease alternatives are provided in Table 3.

- *Can I afford to invest money up front in stand establishment and management costs for the opportunity to make a lot more money down the line?*

  How risk averse are you? If you do not wish to incur substantial costs associated with your forestland for the opportunity to make a generous return in the long run, then the lease option may be the best for you. But, if you can tolerate forgoing money in the present to establish and maintain your forestland for the long-term potential of making substantial returns on your investment, then the self-management option may be best.

- *What are my tax rates (income, property and capital gains)?*

  Differing tax rates may affect the viability of self-management vs. leases. A higher capital gains tax rate relative to income tax rate may make the lease the more viable option. On the other hand, if you are in a high income tax bracket, or if income tax brackets change in the future so that you are moved into a higher tax bracket, then self-management may be the more viable option.

- *What lease price am I being offered vs. the quality of my forestland?*

  A professional forester can help you answer this question. In general, the higher the lease payment offered, the more attractive it will be. You need to measure this against the quality of your forestland, however.

- *Do I have other objectives beside maximizing financial returns?*

  Many landowners have goals other than maximizing the amount of money they make from their forestland. Actions such as enrollment in the Forest Stewardship program, in which one might manage for goals other than profit maximization, or managing purely for aesthetics, recreational values, wildlife values or because of personal ideals regarding the land may preclude one from the lease alternative. Be sure to identify carefully your overall goals for your forestland.

If you do decide to lease your forestland, be sure to consult with professionals before signing the contract. Have an attorney look over the contract to make sure you explicitly understand all provisions, especially penalties that apply if you break the lease early or if the other party breaks the lease early. If there are provisions you are uncomfortable with, do not sign the agreement until you have negotiated with the leasing company. If you are still uncomfortable, don't sign it. It is your land, after all.

In all cases, the value of information cannot be overstated. Consult with as many people as you can regarding your alternatives. Make sure you know with whom you are dealing. Contact groups like the Better Business Bureau and the Louisiana Forestry Association to help you determine the quality of the leasing company. Contact state government organizations, like the Louisiana Department of Agriculture and Forestry and the LSU AgCenter, and private organizations and individuals, like consulting foresters and industry foresters. They can help you make your decision.

Do not reject either alternative out of hand. Both are viable alternatives. The best alternative for you will depend on your individual situation. Good luck and enjoy your forestland!

Table 3. Net present values of lease revenues. NPV is expressed on a per acre basis and are after tax values.

Lease payment ($ per acre)	Net Present Value ($ per acre)
$40	$252.61
$60	$396.39
$80	$540.17
$100	$683.95
$120	$827.74

By comparing Tables 2 and 3, we can draw the following financial conclusions regarding this set of scenarios:

- The $40 per acre per year lease was superior to self-management scenarios 1, 1A, 2, 2A, 3 and 4.
- The $60 per acre per year lease was superior to self-management scenarios 1, 1A, 2, 2 A, 3, 3A, 4 and 4A.
- The $80 per acre per year lease was superior to all self-management scenarios except 5A, 6 and 6A.
- The $100 per acre per year and $120 per acre per year leases were superior to all self-management scenarios.

This is only an example. Everyone's forestland situation is different. Therefore, these numbers should act only as rough overall guidelines, not as the final answer for your individual situation. In all situations, it is always best to consult with professional foresters associated with consulting firms, industry, the LSU AgCenter or the Louisiana Department of Agriculture and Forestry.

In general terms, the higher the site quality, the more likely it is you will receive a high lease offer. You would not expect to receive a $100 per acre lease offer on land that has a poor site index.

So, which is right for you? That will depend a lot on your individual preferences and characteristics. Here are some guidelines:

- *Do I need an annual income from my forestland?*

  If you do, then a lease may be a viable alternative. If you view your forestland more as a long-term investment in which you will receive a lump sum of cash from the sale of timber, then self-management may be the best alternative.

- *Am I willing to have someone else manage my land without my input?*

  If you are, then the lease may be for you. This may be a particularly attractive alternative for absentee landowners who do not have the time to spend overseeing their forestland. When a company enters into a lease arrangement, it has a long-term stake in your land. It will likely oversee your forestland very closely to ensure it is kept intact and free from intruders or mischief.

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