AGEC 429: AGRICULTURAL POLICY

LECTURE 17: ANALYSIS OF PAST FARM BILL PROGRAMS II
The 1996 and 2002 Farm Bills: A Plan to Get Government Out of Agriculture ...that Doesn’t Quite Work!

Where we left off last time:

- **1985 Farm Bill**
  - Target price (deficiency payment) program (**Revenue Support**)
  - Prices increased and everyone expected that trend to continue

- **1990 Farm Bill**
  - Basically extended the target price (deficiency payment) program
  - Some important changes in how the deficiency payment was calculated to reduce government costs of farm programs.
Debate on the 1996 Farm Bill

- Soon after 1990 farm bill was implemented, prices began to drop sharply.

  ![Graph: Prices Received by Farmers, 1980-2006 (1982=100)]

- Then in late 1995, just as the new farm bill was being debated, farm prices increased by nearly 30%! The forecast was for price to continue increasing!

- In 1994, U.S. had just signed a new multilateral trade agreement (WTO) agreeing to eliminate coupled agricultural polices. Why?

- Thus, debate focused on how to ________________________________ by substituting a DECOUPLED policy in place of the COUPLED target price (deficiency payment) program to meet our obligations under the WTO agreement and eventually get government out of the business of supporting agriculture.
Federal Agriculture Improvement and Reform (FAIR) Act of 1996

- Referred to as the “________________” Bill
  Objective: Help farmers transition from dependence on government to dependence on the market.

- First Farm Bill to legislate a policy to ________________________________
rather than policies for each individual program commodity:

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<th>Titles in FAIR ACT of 1996</th>
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<td>I  Agricultural Market Transition Act (AMTA)</td>
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One primary title that applied to MOST program commodities.

An Act within an Act that overturned much of previous farm policy:
- No target prices or deficiency payments
- No annual set-aside programs or other supply controls
- Almost complete planting flexibility

Implemented **fixed, declining, decoupled, Direct Payments to farmers over a 7-year period**
FAIR ACT of 1996

Title I - Agricultural Market Transition Act (AMTA)

- **Fixed, declining** AMTA payments intended to help farmers transition from dependence on government assistance to dependence on the market over a 7-year period.
  - Known by several names:
    1. Production Flexibility Contract (PFC) payments
    2. Agricultural Market Transition Act (AMTA) Payments
    3. “Freedom to Farm” payments
    4. “Direct Payments”

- AMTA payment (direct payment) calculation:
  \[ \text{AMTA payment} = \text{DPR} \times \text{total program output} \times 0.85 \]
  where:
  - DPR is the “direct payment rate” set by the legislation ($/unit)
  - Decoupled direct payments (AMTA) replaced __________ payments (target price deficiency payments)
  - DECOUPLED because payment calculated on BASE (historical) acreage and BASE yield and not current acreage or yield … and price is irrelevant.
  - Almost full planting flexibility. Producers could plant almost anything (except fruits and vegetables) or nothing at all and still get the payment.

- Effort to Reduce Cost of Direct Payments

- Lower DPR each year until it reached zero after 7 years. Then government would be done supporting farm price and income.
Title I – AMTA (continued)

- **Marketing Loan Program (Coupled Payments) Continued**
  - Market-level loan rates (safety net level) *maintained*.
  - Expanded to cover all farmers of covered crops (wheat, feedgrains, rice, upland cotton, soybeans, and other oilseeds) - even those who do not take out NR loans!
  - Instead of forfeiting their crop to the government, farmers keep crop and repay loan at lower market price (or announced “repayment rate”).
    » “Non-recourse” feature became irrelevant for covered crops
    » Provided larger payments as prices dropped

- Gain to farmers **WITH** NR loans called a ______________________.
  » Definition: Marketing Loan Gain (MLG) = $P_L - P_M$
  » The gain to a farmer from being allowed to repay a NR Loan Rate at a lower market price (or “repayment rate”).

- ML payments ALSO to farmers who do **NOT** take out NR loans. These payments are called ______________________.
  » A payment equal to the MLG but to farmers who do NOT take out a NR loan.
  » Only difference between an MLG and an LDP is that an MLG is a payment to farmers **with** NR loans while an LDP is the same payment to farmers **without** NR loans
New Feature of Farm Policy in the FAIR Act of 1996: The Environmental Quality Incentive Program (EQIP)

- EQIP added additional conservation policy instruments:
  - Financial and technical assistance to encourage adoption of farming systems that conserve resources and enhance environmental performance.
  - Cost-share and incentive payments for eligible conservation practices under short-term (1- to 10-year) contracts.
  - Popular EQIP practices include cover crops, nutrient management, forest stand improvement, prescribed grazing, irrigation efficiency improvement, and water quality improvement practices. Implementing conservation practices can lead to cleaner water and air, healthier soil, and better wildlife habitat while improving agricultural operations.

**Pie Chart**

- Animal Waste Management: 24%
- Irrigation Water Management: 27%
- Soil Erosion and Sediment Control: 21%
- Grazing Land: 16%
- Other: 12%
Bad Timing!

- Shortly after the 1996 farm bill (FAIR Act) was signed, farm prices began to drop sharply and continued dropping until early 2002 due to a worldwide recession.

Collapsing prices brought demands for action.
- Most had believed prices would continue going up so farmers did not need deficiency payments anymore.
- When prices began dropping, concern arose that we had been too hasty in eliminating the target price program.

Democrats: “Freedom to Farm” is “___________________”

Republicans: Problem is the _________________, not the policy.
WHAT TO DO?

- Fight between Republicans and Democrats over how to fix the problem:
  - Democrats: Overturn 1996 Farm Bill and revert to traditional instruments for price and income support
  - Republicans: Continue with 1996 Farm Bill and “________________.”

THE COMPROMISE

- Market Loss Assistance Payments (MLA)
  - Greater direct payments to farmers (decoupled) without changing the structure of the 1996 Farm Bill
  - Initially vetoed by Clinton because the MLA idea did not provide enough additional farm income support … but he eventually approved
  - MLA or “_______________________” payments in each year remaining in the 1996 Farm Bill from 1998-2001
  - MLA payments multiplied the direct payments received by producers by a factor of 1.5 to 2.
Government Costs Continue to INCREASE

- Direct Payments (decoupled) declined each year as required in the 1996 Farm Bill (YELLOW)

- But they were more than replaced by MLA (emergency assistance) payments (ORANGE) and growing MLG/LDP payments (RED SHADED).

- Consequently, government payments to farmers actually increased in total instead of decreasing as intended in the 1996 Farm Bill.
Marketing loan program was still in place even though the target price (deficiency payment) had been ________________.

PM was expected to be larger than PL so there would be no government payments.

But as world demand declined, so did the market price... creating MLG/LDP payments...

... that grew larger...

... and larger as demand continued to drop.
2002 Farm Bill Debate

- Debate in 2001 just as prices were hitting bottom.
- Concern that prices would continue falling after Farm Bill expired... but they didn’t!

Meaning that the MLA payments were not actually part of the Farm Bill but made through separate legislation each year.

- MLA payments were __________, __________, and __________.

- Heated debate:
  - Return to higher loan rates and supply controls... or
  - Stay with planting flexibility and decoupled MLA payments?

- U.S. commitments ______________ to shift to less market-distorting policies played a more important and visible role in debate.
Farm Security and Rural Investment Act (FSRIA) of 2002

- Commodity provisions similar to 1996 Farm Bill
- Continued and increased decoupled AMTA (direct) payments (rather than let them decline)
- Continued marketing loan program (MLGs and LDPs)
- Introduced a New Revenue Payment Program:
  Counter-Cyclical Payments (CCPs)
  - Similar to the target price/deficiency payment program that was terminated with the 1996 Farm Bill
  - Re-introduced target prices and revenue support to producers
  - Intended to be a permanent mechanism to make income transfers to producers automatically when prices are low rather than to pass special “emergency” legislation in low price years like the MLA.
  - For all covered crops plus dairy

- Allowed farmers to update their acreage bases and program yields:
  - First time in many years.
  - Some whole areas had switched to other crops (e.g. from corn to cotton) but still getting payments on old base and program yield (e.g. corn).
Other Major Provisions of FSRIA of 2002

- ________________ Labeling (COOL) for meat, fish, produce and peanuts required by 2004:
  - Meat products can be labeled as U.S.-made only if the animals were born, raised, and slaughtered in the U.S.
  - Requires labeling on each constituent part as to country of origin. (Bag of salad?)
  - Costs of tracking origin of all components are very high.
  - Huge debate so implementation was delayed.
  - Rules re-written by USDA and finally implemented on March 16, 2009.

- Added an “______________” Title for the first time
  - First time energy policy included in a farm bill
  - Committed $405 million to the development of ethanol and biodiesel fuels

- Added new “Conservation Security Program” (see next page)

- EQIP funding increased 6 fold

- Additional commodities eligible for loans:
  all covered crops plus extra long staple cotton, wool, mohair, honey, dry peas, lentils, and small chickpeas.
Other Major Provisions (continued)

- **Conservation Security Program (CSP)**
  - New program providing payments to land owners for implementing practices on working lands that address one or more resources of concern, such as soil, water, or wildlife habitat.
  - Wide range of practices can be subsidized.
  - Producers must develop and submit a conservation plan to USDA that identifies the resources and designated land to be conserved.
FSRIA of 2002

FSRIA 2002 Programs Operated like a Combined CCP/Marketing Loan Program

- Covered crops (new name for “program crops”) which are the crops eligible for income support programs:
  wheat, corn, grain sorghum, barley, oats, upland cotton, rice, soybeans and other oilseeds (sunflower seed, rapeseed, canola, safflower, flaxseed, mustard seed)

- CCP program
  - looks like the old target price (deficiency payment) program except...
  - farmers receive only 85% of the payment (now called CCP payment) ...
  - after subtracting out the Direct Payment.

- Marketing Loan Program
  - Famers receive Marketing Loan Gain/Loan Deficiency Payments (MLG/LDP).

- Market Sales Revenue
  - Rest of farm revenue comes from farm sales.
2002 Farm Bill Payment Calculations

Direct (Decoupled) Payments:

\[ DP = DPR \times (\text{base acres} \times 0.85) \times \text{farm program yield} \]

Counter Cyclical Payments (Partially Decoupled):

\[ CCP = (P_T - \max(P_M \text{ or } P_L) - \text{DP payment rate}) \times (\text{base acres} \times 0.85) \times \text{farm program yield} \]

MLG/LDP Payments (Coupled):

\[ MLG/LDP = (P_L - P_M) \times \text{actual acreage} \times \text{actual yield} \]

Total Payments to Farmer:

\[ TP = DP + MLG/LDP + CCP \]

Market Sales Revenue of Farmer:

\[ MR = P_{Market} \times \text{Quantity Sold} \]

Total Revenues of Farmer:

\[ TR = TP + MR \]

Check out IIFPP1.xls to see if the calculation for cotton is correct.

- Then play with the price level and see how amounts from market, CCP, LDP/MLG, and DP change.
FSRIA of 2002

Calculating Government Payments Under FSRIA 2002

Example for Cotton Farmer

Assume:

\[
\begin{align*}
\text{PT} &= \$0.724/\text{lb} \quad \text{Base acreage} = 100 \text{ acres} \\
\text{PL} &= \$0.520/\text{lb} \quad \text{Program yield} = 500 \text{ lbs/acre} \\
\text{PM} &= \$0.420/\text{lb} \quad \text{Actual acreage} = 150 \text{ acres} \\
\text{DPR} &= \$0.0667/\text{lb} \quad \text{Actual yield} = 530 \text{ lbs/acre}
\end{align*}
\]

- **Direct Payments (DP)**
  - Same formula as used in the 1996 Farm Bill:

\[
\text{DP} = \text{direct payment rate} \times (\text{base acres} \times 0.85) \times (\text{farm program yield})
\]

\[
\begin{align*}
\text{DP} &= \$0.0667 \times (100 \times 0.85) \times 500 \\
\text{DP} &= \$2,834.75
\end{align*}
\]

- DPs are ______________from current production and price
Counter-Cyclical Payments

- Formula for calculating CCPs similar to the calculation of a deficiency payment except direct payment rate must be subtracted out.

\[ \text{CCP} = (P_T - \text{Max}(P_M \text{ or } P_L) - DPR) \times (\text{base acres} \times 0.85) \times \text{program yield} \]

Using the data assumptions for cotton:

\[ \text{CCP} = (0.724 - \text{Max}(0.42 \text{ or } 0.52) - 0.0667) \times (100 \times 0.85) \times 500 \]
\[ \text{CCP} = (0.724 - 0.52 - 0.0667) \times 85 \times 500 \]
\[ \text{CCP} = 0.1373 \times 42,500 \text{ lbs} \]
\[ \text{CCP} = $__________ \]

- CCPs decoupled from production (but not price) - _________________
  - Farmer has nearly complete flexibility in what to plant to his base (fruits and vegetables still not allowed).
  - Could even leave land idle and still get the CCP payments.
Calculating Government Payments Under FSRIA 2002 (cont’d)

- **Market Loan Gain/Loan Deficiency Payments:**
  - Same as under the 1996 farm bill (standard calculation):
    \[ \text{MLG/LDP} = (P_{\text{Loan}} - P_{\text{Market}}) \times \text{actual acres} \times \text{actual yield} \]

  Using the assumptions for cotton:

  \[ \text{MLG/LDP} = (0.52 - 0.42) \times 150 \times 530 \]
  \[ \text{MLG/LDP} = 0.10 \times 79,500 \text{ lbs} \]
  \[ \text{MLG/LDP} = $\underline{8,950} \]

- **MLG/LDP payments are ________________________________**
  - Payments depend on both the level of actual (current) production and the level of actual (current) price
Calculating Government Payments Under FSRIA 2002 (cont’d)

- Total Payments to Farmer:

  Total Payment (TP) per Farmer = DP + LDP/MLG + CCP

- Total Revenue of Farmer:

  - The sum of total payments (TP) plus market sales revenue
  
  - Total Revenue of Farmer = TP + (PM x Quantity Sold)

Example of Total Revenue of the cotton farmer:

\[
\begin{align*}
\text{CCP} &= \$5,835.25 \\
\text{DP} &= \$2,834.75 \\
\text{MLG/LDP} &= \$7,950 \\
\text{Market Sales} &= PM \times \text{Quantity Sold}
\end{align*}
\]

Total Revenue = DP + CCP + MLG/LDP + Market Sales
Total Revenue = \$2,834.75 + \$5,835.25 + \$7,950 + \$33,390
Total Revenue = \$50,010