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Farm Commodity Programs: A Short Primer

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Summary

The U.S. Department of Agriculture (USDA) is required by law to subsidize more than two dozen specified agricultural commodities. Omnibus farm legislation in 1996 was intended to usher in a new system of price and income supports for many of these commodities by accelerating the shift toward a more “market-oriented” agricultural policy and by gradually reducing financial support. However, unanticipated declines in export markets and farm prices led Congress to enact a series of supplemental measures from 1998 through 2001 that provided additional *ad hoc* support for producers, greatly increasing the cost of commodity assistance. A new farm bill, the Farm Security and Rural Investment Act of 2002 (P.L. 107-171), is intended to avert the need for *ad hoc* measures, largely by expanding several existing support programs and adding new ones.

Overview

USDA commodity and price support programs represent the heart of U.S. farm policy, by virtue of their longevity – they have existed since the early 1930s – and their cost. Net outlays for the Commodity Credit Corporation (CCC), USDA’s program financing mechanism, have averaged about \$16 billion annually from FY1996 to FY2002.¹

Standing authority for USDA-CCC programs is provided mainly by three permanent laws: the Agricultural Adjustment Act of 1938 (P.L. 75-430), the Agricultural Act of 1949 (P.L. 81-439), and the CCC Charter Act of 1948 (P.L. 80-806). Congress frequently alters provisions of these laws through omnibus, multi-year farm bills, and various budget measures. The previous farm bill, covering programs through 2002, was the 1996 Federal Agriculture Improvement and Reform Act (P.L. 104-127). “Emergency” farm laws

¹ USDA’s Farm Service Agency (FSA) delivers CCC-funded commodity program benefits through a network of local (“county”) offices overseen by committees of elected farmers.

enacted in 1998, 1999, 2000, and 2001 (P.L. 105-277, P.L. 106-78, P.L. 106-224, P.L. 107-25) provided temporary supplemental aid for major commodities.²

The newest omnibus farm law, the Farm Security and Rural Investment Act of 2002 (P.L.107-171), is intended to avert the need for such supplemental aid. It expands several existing support programs and adds new ones, notably new “counter-cyclical” support available when farm prices for major crops and for milk decline beneath statutorily prescribed levels. This law is effective from 2002 through 2007.

Current law requires USDA to offer support for wheat, feed grains (corn, sorghum, barley, oats), cotton (upland and extra-long staple–ELS), rice, soybeans, other oilseeds (sunflower seed, canola, rapeseed, safflower, flaxseed, mustard seed), milk, peanuts, beet and cane sugar, wool, mohair, honey, dry peas, lentils, small chickpeas, and tobacco.

These commodities accounted for approximately \$75 billion, or 37%, of all farm cash receipts in 2001. Other commodities that normally receive no direct support include meats, hay, poultry, fruits, nuts, vegetables, and nursery/greenhouse products. But even producers of these items can be affected by farm policy decisions, either because such producers also raise some price-supported commodities, or because Government intervention in one farm sector can influence production and prices in another sector.³

Statutorily Required Support

Policymakers have devised a variety of program methods for the CCC to assist producers, each generally designed to achieve these broad objectives:

- To ***supplement farmer incomes***. Tools include annual *fixed decoupled payments* and *counter-cyclical deficiency payments* for grains, cotton, oilseeds, and peanuts; *counter-cyclical deficiency payments* for milk; and *nonrecourse marketing loans* and *loan deficiency payments* for grains, cotton, peanuts, oilseeds, wool, mohair, honey, dry peas, lentils and small chickpeas;
- To ***manage supplies and support commodity market prices***. *Marketing quotas/acreage allotments* for tobacco, and *marketing allotments*, for sugar, are available to restrict output. *Surplus purchases* help support farm prices for milk and various specialty crops.

The types and levels of support employed vary by commodity. Some are supported by only one method; others receive their support through a combination of program tools.

² Most of these acts also provided separate funds for disaster losses. See CRS Report RL31905, *Emergency Spending for Agriculture: A Brief History of Congressional Action, FY1989-2001*.

³ Although such commodities generally do not receive mandatory support under CCC price and income support programs, Congress or the Administration often provide periodic assistance to them. For example, the 2002 farm law requires USDA to pay apple growers \$94 million to cover 2000 market year losses, and to spend \$200 million annually to purchase fruits, vegetables, and specialty crops under the Section 32 program. See also “USDA Discretionary Support,” page 5.

Wheat, Feed Grains, Upland Cotton, Rice, Peanuts, Soybeans, and Other Oilseeds. Eligible producers (those with past production histories for these crops) can receive *fixed, decoupled payments* each year (see rates in table); along with *counter-cyclical deficiency payments*, which make up the difference between the crop's average market price plus the fixed payment and its "target price" (see table), which is pegged to past production. Both payments to a producer are based on 85% of the farm's past production history, i.e., past acreage planted times per-acre yield, calculated under formulas in the 2002 farm law. Payment recipients can plant almost any combination of crops on their land; they are not bound by the annual, USDA-imposed supply management rules for each crop in effect prior to 1996. Some restrictions do exist: for example, land generally cannot be replanted to fruits and vegetables, and conservation rules must be followed, on subsidized farms.

Crop	Loan Rates	Fixed Decoupled Payment Rates	Counter-Cyclical Target Prices
	2002/03, 2004/07 *	2002-2007	2002/03, 2004/07 *
Wheat, \$/bu	2.80, 2.75	0.52	3.86, 3.92
Corn, \$/bu	1.98, 1.95	0.28	2.60, 2.63
Sorghum, \$/bu	1.98, 1.95	0.35	2.54, 2.57
Barley, \$/bu	1.88, 1.85	0.24	2.21, 2.24
Oats, \$/bu	1.35, 1.33	0.024	1.40, 1.44
Cotton, \$/lb	0.52, 0.52	0.0667	0.724, 0.724
Rice, \$/cwt	6.50, 6.50	2.35	10.50, 10.50
Soybeans, \$/bu	5.00, 5.00	0.44	5.80, 5.80
Other oilseeds, \$/lb	0.096, 0.093	0.008	0.098, 0.101
Peanuts, \$/ton**	355	36	495

* Reflects rates that change in some years. **Peanut quotas were ended by 2002 law; quota holders also are receiving \$220/ton/year for 5 years as compensation.

Producers, regardless of whether they receive the above payments, also are eligible for *nonrecourse marketing assistance loans* and *loan deficiency payments*. (See table for rates.) To qualify, a farmer pledges the stored crop as collateral. Nonrecourse loans generally must be repaid with interest within 9 months or else the producer forfeits the pledged commodity to the government, which has "no recourse" other than to accept it in lieu of money. However, two features are intended to help avert forfeitures, and subsequent buildup of CCC-owned surpluses. First, the "marketing loan" feature enables the farmer to repay the loan at a USDA-calculated rate approximating market prices. If that repayment rate is below the original USDA loan rate, the farmer captures the difference as a subsidy (marketing loan gain). Loan deficiency payments (equal to marketing loan gains) also are available to eligible producers who choose *not* to take out

a crop loan. (See Grains, Cotton, and Oilseeds: Farm Bill Policy in the CRS Electronic Briefing Book on Agriculture Policy and Farm Bill.)

ELS Cotton, Wool, Mohair, Honey, Dry Peas, Lentils, and Chickpeas.

Producers of these commodities are not eligible for fixed decoupled or for counter-cyclical payments, but can receive *nonrecourse marketing assistance loans* and (except for ELS cotton) *loan deficiency payments*. Loan rates are specified in the 2002 farm law.

Tobacco. The tobacco program, intended to be operated at no net government cost, operates through a combination of *mandatory marketing quotas* and *nonrecourse loans*. Marketing quotas limit the amount of tobacco each farmer can sell, which indirectly raises market prices. The loan program establishes guaranteed minimum prices. (See CRS Report 95-129, *Tobacco Price Support: An Overview of the Program*.)

Sugar. A combination of *import quotas* and *nonrecourse loans* is intended to support prices at 18¢/lb.(raw cane) and 22.9¢/lb. (refined beet), at no net cost to the government. *Marketing allotments* limit production to avoid loan forfeitures and CCC costs; also authorized are payments (in the form of CCC-owned sugar) to farmers who agree to *acreage reduction*. (See CRS Issue Brief IB95117, *Sugar Policy Issues*.)

Milk. Price support is provided through surplus *commodity purchases*. The CCC buys bulk cheese, butter, and nonfat dry milk from dairy processors unable to sell them on the private market for at least the prices offered by the CCC. These prices are set so that processors will, in turn, pay farmers a milk price that reflects at least the federally mandated support, currently \$9.90 per cwt. A new “National Dairy Program” offers *counter-cyclical payments* equal to 45% of the difference between \$16.94 and the Boston Class I (fluid use) price, whenever that price is lower than \$16.94; each farmer’s payments are limited to 2.4 million lbs. of annual production (approximately a 120-140-cow herd). (See CRS Issue Brief IB97011, *Dairy Policy Issues*.)

USDA Discretionary Support

In addition to the explicitly-required subsidies described above, federal law has long given USDA the discretion to offer support for virtually any farm commodity. Recent examples have included *direct payments* of up to \$10 per head for **hogs** in 1999, and of up to \$8 per head for **lambs** (under a 3-year lamb meat adjustment assistance program). Authority and funding for these various activities can come from a number of sources, including CCC (e.g. under the CCC charter act) and Section 32.

Section 32 (of P.L. 320, a 1935 law) permanently appropriates the equivalent of 30% of annual customs receipts to support the farm sector through a variety of activities. Most of this appropriation (now about \$6 billion per year) is transferred directly to USDA’s child nutrition account to fund school feeding and other programs. However, Section 32 also provides USDA with a source of discretionary funds (of which up to \$500 million annually can be carried over each year), which it uses for “emergency removals” of surplus agricultural commodities, disaster relief, or other unanticipated needs. USDA annually purchases hundreds of millions of dollars in meats, poultry, fruits, and vegetables under Section 32 each year. (See CRS Report RS20235, *Farm and Food Support Under USDA’s Section 32 Program*.)

Payment and Loan Limitations

Most commodity subsidies are tied to units produced; therefore, higher output (sometimes past, sometimes current, depending upon the subsidy) means higher benefits, with some limits. For grains, cotton, and oilseeds, the law sets an annual ceiling for fixed decoupled payments at \$40,000 per person, plus a separate annual ceiling for counter-cyclical payments at \$65,000 per person. A separate payment limit of \$75,000 per person applies to marketing loans gains for these crops and for dry peas, lentils and chickpeas.

Because an individual can receive *half*-payments on two additional farms, the effective annual cap on total combined payments actually has been \$360,000 per person. Limits apply to individuals rather than farm units; thus, a single farm with multiple owners/operators might receive much more than the above amounts. Also, there is no per-person monetary limit on the volume of crops that can be put under CCC loan, or on how much can be forfeited in lieu of loan repayment. Finally, marketing loan gains in the form of USDA-issued commodity certificates (which farmers immediately redeem to satisfy loan repayments) are not counted toward the \$75,000 loan cap. Peanuts have separate payment caps, as do wool, mohair, and honey. (See Commodity Program Payment Limits Under the 2002 Farm Bill in the CRS Electronic Briefing Book on Agriculture Policy and Farm Bill.)

Policy Discussion

When the commodity programs were first authorized in the early 1930s, most of the Nation's 6 million farms were diversified and small (by today's standards). There was a perceived need to address the severe economic problems then faced by this large segment of society, where about 25% of the U.S. population then resided. Moreover, it was argued, stabilizing the agricultural sector – through guaranteed minimum farm prices, income payments to producers, and/or various supply management techniques – would help to ensure an abundant supply of food and fiber at reasonable prices in the future.

Since then, farming has changed significantly. Most commercial agriculture is now confined to fewer, larger, and more specialized operations. In 1997 (the last farm census year) about 157,000 large farms, with annual agricultural sales averaging about \$900,000, accounted for 8% of all U.S. farms but 72% of all farm sales. Most of the nation's 2 million farms are mainly part-time, where operators rely on off-farm sources for most of their income. Farm residents now account for less than 2% of the total U.S. population.

Also, the economic health of farmers has become increasingly tied to the needs of processors and marketers, and to global markets. Critics have long argued that U.S. commodity-based policies are outdated and may even be detrimental to modern agriculture, and to society in general. Although the programs have retained many features dating to the 1930s, they also have evolved – in response both to the changes occurring in agriculture and the economy, and to budgetary and trade pressures. At issue is whether they have evolved quickly enough, or in the most appropriate ways.

Congress and the Administration sought, for many decades, to steer price and income support programs onto a more “market-oriented” course, so that producers would look to the private market rather than the government for economic rewards from production

agriculture. A succession of farm bills, particularly since the 1970s, moved farm policy in this direction, mainly through incremental changes in existing programs. The 1996 farm law, written at a time of high farm prices and expanding exports, was aimed at accelerating the programs' market orientation. Analysts anticipated that CCC net outlays under the 1996 law would average less than \$6 billion yearly, compared with \$15 billion yearly during the 1980s and \$10 billion in the early 1990s.

However, unanticipated declines in export markets and in farm prices both drove up the cost of programs already authorized by the 1996 farm law (primarily marketing loans and loan deficiency payments), and also led Congress to enact, between 1998 and 2001, more aid. About \$30 billion in emergency farm and related assistance was approved, of which some \$22 billion was in response to falling commodity prices (the rest was natural disaster aid). For *calendar* 2000 and 2001, direct farm payments reached a total of \$22.9 billion and \$21.1 billion, respectively – representing 49% and 43% of net farm income for each year. CCC net outlays for *all* farm-related programs and activities reached a record \$32.3 billion in *fiscal* year 2000. They declined to \$22.1 billion in FY2001.

Record-high subsidies helped the farm economy as a whole remain in relatively strong financial condition in recent years. However, most policymakers and farm groups sought a new farm law that would preclude the need for future ad hoc assistance bills. This led to adoption, in the 2002 law, of new counter-cyclical assistance whereby subsidies (for grains, cotton, oilseeds, and milk) automatically increase when farm prices decline, and decrease when they rise.

This and other commodity provisions in the law have attracted widespread criticism from those here and abroad who view them as reversing the market-oriented course Congress had charted for long-term farm policy in 1996. These critics argue that the bill perpetuates outmoded, commodity-oriented policies that tie support to the prices of a few major row crops; with legislated target prices and loan rates set well above market prices, U.S. producers will continue to over-produce supported commodities, distorting market prices and global trade. CCC outlays are now projected to average \$17-20 billion annually – and perhaps more – through FY2007, at a time of a deepening federal deficit and more pressing national priorities, they argue. Furthermore, the adoption of expanded farm subsidy programs has undermined U.S. credibility in world trade negotiations, where the United States has called on other countries to reduce their own trade distorting agricultural subsidies, they contend.

Supporters counter that the bill's commodity title provides needed support to farmers who otherwise would see plunging incomes and asset (e.g., land) values due to continuing poor price and market conditions worldwide. The bill maintains market orientation by continuing to give farmers the flexibility to plant crops based on market signals unbound by government supply management rules. The measure fully complies with congressional spending limits, and will provide no more in subsidies than farmers received under the last omnibus farm law as supplemented by the emergency farm measures, they note. The new law contains a new "circuit breaker" that requires USDA to cut trade-distorting subsidies in order to remain within the \$19.1 billion limit on such spending under the Uruguay Round Agreement on Agriculture. And, the United States will be in a stronger position to negotiate new agricultural trade reforms: the United States should not unilaterally cut its own subsidies until foreign competitors reduce their own often higher subsidies, as well as their barriers to U.S. farm exports, supporters contend.