

Update on the 2007 Farm Bill

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INTRODUCTION

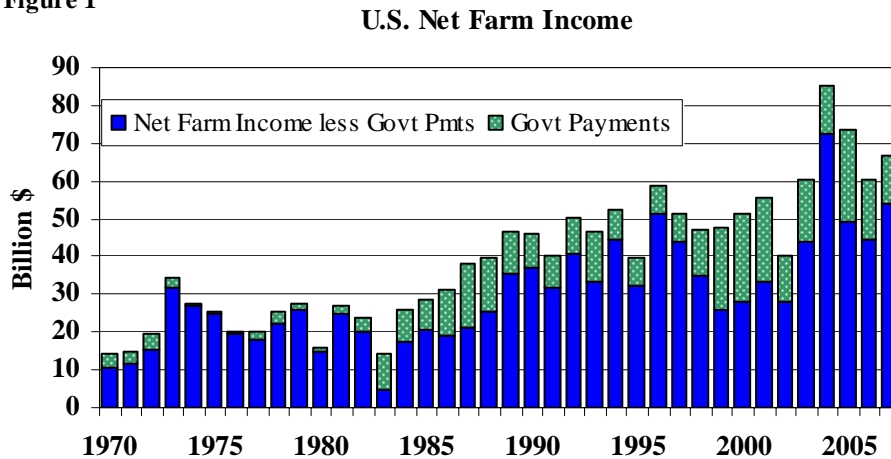
Farm bills reflect the tenor of the times, and these are interesting times in agriculture. A variety of forces are aligning to shape the future of U.S. agriculture. The immediate future looks brighter for some, but perhaps dimmer for others. In this environment, Congress is writing legislation to replace the expiring 2002 Farm Bill. Will this legislation be similar to previous farm bills, or a major departure? Will there be a new farm bill at all? It is still too early to tell, but an extensive set of concepts and proposals for the next farm bill have been made. While the final direction of the new farm bill is still unknown, the development of the new farm bill will continue to be shaped in part by the setting for the debate, including the economic climate, the budget situation, the trade arena, and of course, the political landscape.

DRIVERS OF THE DEBATE

The Economic Climate

Two primary factors drove the formation of the 2002 Farm Bill. The first factor was that U.S. commodity program crops were coming off four years of low prices due to increased supplies and softened world demand. Since then, the U.S. economy has experienced sustained growth, and record farm income of \$85 and \$74 billion was realized in 2004 and 2005. The most recent forecast by USDA predicts that U.S. net farm income in 2006 dropped to \$60.6 billion, but will rebound to \$66.6 billion in 2007 (Figure 1). Income in both 2006 and 2007 are above the 10-year average (1998-2007) of \$58.9 billion. On a nominal basis, the 2004-2007 period will represent the strongest U.S. farm income performance on record. However, over that same period of time, government payments were responsible for an annual average of \$16.5 billion (23.4%) of net farm income.

Figure 1

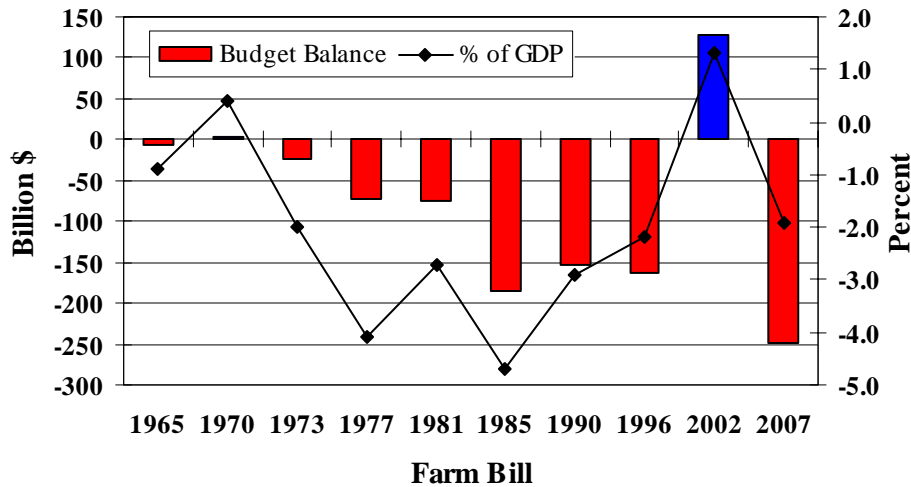


The high farm incomes, coupled with the cost farm subsidies the last few years has led to calls to 1) to end farm income support programs as unnecessary, 2) to strengthen programs and raise the level of the safety net under current higher prices, 3) to modify current programs to create a more effective and/or equitable safety net, or 4) to simply extend the current safety net.

The Budget Situation

The second factor that drove the formation of the 2002 Farm Bill was a budget surplus. However, recent record federal budget deficits have raised concerns among agricultural interest groups that farm programs could be cut in an effort to reduce deficit spending. The deficit of \$248 billion in fiscal year 2006 (matched up as the lead-in year of the 2007 Farm Bill debate) is the largest ever amidst a farm bill debate, but is significantly lower than deficits in recent years and previous estimates for 2006. Figure 2 shows the federal budget balance and balance as a percent of U.S. gross domestic product (GDP) in each year prior to passage of a Farm Bill from 1965 to 2007. Budget surpluses existed only twice during this time period—1969 and 2001. Also, the current budget deficit represents only 1.9 percent of GDP and is comparatively lower than the deficit at the time of most farm bill debates since the mid-1970s.

Figure 2



While the budget deficit may not be a major issue from an historical perspective, budget rules adopted by Congress have made it a major issue. The “Pay-As-You-Go” (PAYGO) budget rules adopted in the U.S. House of Representatives stipulate that any bill that offers provisions that increase spending from Congressional Budget Office (CBO) budget baseline estimates be offset by spending cuts (or tax increases) in other provisions. For commodity programs, the PAYGO rules are important for two reasons. First, it makes it difficult to increase spending beyond the CBO baseline. Second, it makes the CBO baseline the primary factor for determining how much funding will be available for commodity and other farm bill programs.

Every year CBO estimates the cost of current government programs 10 years in the future. That estimate becomes the baseline for how much money will be allowed to be spent on a particular program in succeeding years. Since current estimates forecast higher crop prices over the next few years, farm program payments are expected to decrease. As shown in Table 1, recent CBO estimates project that spending on commodity programs over the next six years (2008-2013) will be \$30 billion, or 42 percent less it was over the previous six years (2002-2007). Consequently, the budget baseline (i.e., the total amount of money the Agriculture Committees in Congress have fund farm bill programs) will be reduced relative to previous years. The House and Senate Budget committees provided “reserve” funds of \$20 and \$15, respectively for 2007 Farm Bill programs, however, those funds will not be available unless spending offsets can be identified, or House and Senate leaders agree to waive PAYGO rules.

Table 1. Actual and Estimated Cost of Commodity Programs for the 2002 and 2007 Farm Bills (Billion \$).

2002 Farm Bill		2007 Farm Bill	
FY2002	13.16	FY2008	7.20
FY2003	12.13	FY2009	7.31
FY2004	8.02	FY2010	6.99
FY2005	14.12	FY2011	6.85
FY2006	16.90	FY2012	6.95
FY2007	8.60	FY2013	7.15
Total	72.93	Total	42.45

Source: Congressional Research Service, *Farm Bill Budget and Costs: 2002 vs. 2007*

The Trade Arena

Two events have combined to make trade an important issue in the current farm bill debate. The first issue is the status of the World Trade Organization (WTO) Doha Round negotiations, and the second is the Brazilian litigation in the WTO against the U.S. cotton program. While it can be argued that these issues are currently less important than they were previously, they will still have an impact on the farm bill debate.

For a brief review on the WTO Doha Round negotiations, in a framework agreement in July 2004, WTO members agreed to do three things in regard to agriculture: 1) increase market access (i.e., reduce tariffs that discourage imports), 2) reduce trade-distorting domestic subsidies, and 3) eliminate export subsidies. The difficulty in reaching a full agreement revolves around how these objectives are to be met. How much will tariffs and domestic subsidies be reduced? What is the timeframe for these reductions? The goal was to work these details out by the WTO summit in Hong Kong in December 2005. Since all 149 WTO members must approve any agreement, and there are often numerous competing interests within each nation, reaching a meaningful agreement has proved to be a difficult task. Consequently, an agreement was not reached in Hong Kong, and formal talks were suspended in July 2006 as progress was virtually non-existent. Informal talks among nations and groups of nations have continued from that point, but a major breakthrough appears to be a long way off.

It may be more difficult for the U.S. to negotiate global international trade agreements in the future because 1) the President's trade promotion authority (TPA), which gives the President power to negotiate trade agreements without amendments from Congress, was allowed to expire in July 2007, and 2) the election of a Democratic Congress is less likely to be interested in pursuing free trade agreements.

However, if a trade agreement is not reached, it is likely that the U.S. will face more litigation within the WTO. The Brazilian case in the WTO against the U.S. cotton program set some important precedents that are likely to encourage others to pursue WTO cases against other U.S. commodities. As an example of this, Canada recently filed a complaint within the WTO against U.S. commodity programs, arguing that the U.S. has violated spending limits for trade distorting subsidies in 6 of the last 8 years. Brazil has also filed a similar complaint.

In addition, there are some aspects of the Brazilian cotton case that have not been settled. First, it was determined by the WTO that the U.S. direct payment program is not a "green box" (minimally trade distorting) program. Rather, it is an "amber box" program that has more significant trade distorting aspects, because there is a restriction on planting fruits and vegetables on those acres that receive direct payments. This issue will have to be addressed by Congress should they deem it important to make direct payments a green box program. It is also significant because it increases the likelihood that the U.S. may be in violation of previous trade agreements.

Second, it was also determined that U.S. cotton subsidy programs tied to price—the marketing loan and counter-cyclical payment programs, caused "serious prejudice" to Brazilian cotton producers. The WTO ruling found that these programs encouraged U.S. farmers to produce more cotton than the world was demanding. That cotton was sold on the world market, resulting in lower prices for cotton producers around the world, including Brazil. The U.S. was ordered to remedy this situation, but was given no specific instructions how to do so, and has yet to follow through with this requirement. Should the U.S. fail to address this issue, Brazil may be permitted to seek retaliation within the WTO.

The Political Landscape

The election of a Democratic House and Senate raises some questions about the shape of a new farm bill. The farm policy debate, following the general political environment, has become increasingly partisan. Will Democrats and Republicans follow through on early pledges to work in a bipartisan manner? Will the political power shift in the Agricultural Committees of Congress result in a similar shift in commodity power from South to North? After offering an extensive set of farm bill proposals, how much of a role will the Bush Administration play in the remainder of the farm bill debate? These are just a few of many questions that come to mind when discussing the political setting for the next Farm Bill.

Politicians are not the only force determining the political landscape for the upcoming Farm Bill. Historically, farm groups have generally been united in support of farm bill programs. That united front may be diminishing as there appears to be growing divisiveness among agricultural interest groups and commodity/geographic sectors—especially as farm program funding concerns emerge. Different agricultural interest groups also view farm legislation differently. Obviously, commodity groups that receive direct assistance are going to view those programs differently than those who do not receive direct payments. Likewise, the commodities that receive support have different opinions regarding the value of specific programs. Fruit and vegetable producers have made calls for increased spending on research & development that would benefit them in return for increased competition they may face if changes are made in farm programs to come into WTO compliance. Those raising livestock have also expressed an interest in being included in some heightened fashion in the upcoming Farm Bill.

In recent Farm Bills, nutrition and food assistance interests have played a key role in developing a coalition to pass Farm Bills. Similarly, environmental groups have been generally supportive of the conservation aspects of Farm Bills. However, the willingness of some of these groups to be supportive of commodity programs in the Farm Bill to meet their own interests may be waning. For example, some in the nutrition arena are beginning to question why the U.S. is subsidizing food and feed grains and not “more nutritious” fruits and vegetables.

A much more vocal critic of current commodity programs is the Environmental Working Group (EWG). Although not opposed to government support of agriculture in general, EWG and other conservation advocates (American Farmland Trust, Environmental Defense, etc.) would like to see the money spent on commodity programs allocated to conservation. The 2002 Farm Bill has been widely regarded as the “greenest” Farm Bill to date. In addition to existing conservation programs like the Conservation Reserve Program (CRP) program, funding was increased for the Environmental Quality Incentive Program (EQIP), and the Conservation Security Program (CSP) was established. However, conservation program spending, especially for the CSP, has been a target for Congress when spending cuts have been required to offset disaster payments or as part of budget reconciliation.

Other outspoken critics of U.S. farm supports include anti-poverty groups like the British-based Oxfam. Taking their cue from Brazil and their case against the U.S. cotton program, these groups argue that domestic support for agriculture in the U.S. and other major subsidizing countries is a source of poverty in developing countries. Mainstream media have joined the assortment of groups questioning U.S. farm programs as well. In articles and editorials ranging from exposes on who receives payments to assertions that subsidies are having a negative impact on the taste of food in the U.S., there seems to be no shortage of people speaking out on U.S. farm programs. Certainly this coverage is more negative than with past Farm Bills. However, although there are currently some differences among agricultural interest groups, there is still broad support among farmers, farm organizations, and their Congressional representatives for the farm programs in the 2002 Farm Bill.

THE HOUSE FARM BILL

In July, the U.S. House of Representatives debated and passed its version of the 2007 Farm Bill. Overall, the *Farm, Nutrition, and Bioenergy Act of 2007* from the House is very similar to the 2002 Farm Bill. Leading up to the action of the House Agriculture Committee, it was questionable whether the farm legislation in the House would be similar to the 2002 Farm Bill, or a vast departure. Proposals were made to reduce some commodity program payments to fund other priorities in the commodity, conservation, nutrition, and energy titles. For instance, in the original Chairman's mark, a proposal was made to reduce direct payments to fund a rebalancing of target prices and loan rates. Similar proposals have been made to fund other programs outside the commodity title. As the legislative process moved along in the House Agriculture Committee, it was apparent that massive reforms to farm policy were not in order. Following is a brief description of primary components of the House version of the 2007 Farm Bill, including the major changes that were made.

Commodity Programs

In the policy world of options and consequences, one option is always to maintain the status quo. For federal farm programs, that implies re-authorizing or extending the basic three-part farm income safety net established in the 2002 Farm Bill. That safety net includes direct payments, marketing assistance loans, and counter-cyclical payments that work together to provide income protection.

The House bill maintains the three part safety net with no changes in the direct payment program, minor changes in loan rates for some commodities in the marketing loan program, and minor changes in target prices for the counter-cyclical program. Changes in loan rates and target prices from 2002 to 2007 are shown in Table 2. Loan rates increased for wheat, barley, oats, and minor oilseeds while loan rates for all other commodities remained unchanged. Target prices also increased for wheat, barley, oats, soybeans, and minor oilseeds. Cotton was the only crop to have its target price reduced.

Table 2. Proposed Target Prices and Marketing Loan Rates in the U.S. House Farm Bill.

Commodity	Target Prices		Marketing Loan Rates	
	2002 Farm Bill	2007 Farm Bill	2002 Farm Bill	2007 Farm Bill
Corn (bu)	\$2.63	\$2.63	\$1.95	\$1.95
Sorghum (bu)	\$2.57	\$2.57	\$1.95	\$1.95
Barley (bu)	\$2.24	\$2.73	\$1.85	\$1.95
Oats (bu)	\$1.44	\$1.50	\$1.33	\$1.39
Wheat (bu)	\$3.92	\$4.15	\$2.75	\$2.94
Soybeans (bu)	\$5.80	\$6.10	\$5.00	\$5.00
Minor oilseeds (lb)	\$10.10	\$11.50	\$9.30	\$10.70
Rice (cwt)	\$10.50	\$10.50	\$0.52	\$0.52
Upland cotton (lb)	\$0.7240	\$0.70	\$6.50	\$6.50
Peanuts (ton)	\$495.00	\$495.00	\$355.00	\$355.00

Revenue Counter-Cyclical Payment Option

The most significant change made in the commodity title of the House farm bill is the option for producers to choose to enroll in a revenue-based counter-cyclical program (RCCP) instead of the current price-based counter-cyclical program (PCCP). The RCCP adopted by the House is basically the same program proposed by USDA in its 2007 Farm Bill proposal in January. The only difference between the House RCCP and the USDA RCCP is that the House version incorporates the adjusted target prices in the House bill.

Economically, there is a strong argument for a redesigned safety net that more effectively focuses on a bottom line revenue or net farm income goal instead of programs that focus largely on price. With two of the three commodity safety net programs tied to price, it is fair to say that producers of commodity program crops should be well covered in low price environments. But does that imply that the safety net is now sufficient? Given the fact that an average of \$1.3 billion in crop disaster aid has been paid out annually from 1999-2006 suggests that the current combination of safety net programs is not sufficient. The primary problem with safety net programs that are tied to price is that they are not very effective in high price/low yield environments. As a result, several proposals have been made to convert the counter-cyclical payment program from one that triggers payments based on price to one that triggers payments based on revenue.

The House RCCP works in the following manner. Payments would be triggered when actual national revenue per acre falls below the national target revenue per acre. The national target revenue is calculated by multiplying the national Olympic average yield (excluding the high and low years) of each program commodity for 2002-2006 by the effective target price for the commodity. The effective target price equals the PCCP target price minus the direct payment rate. The actual national revenue per acre is calculated by multiplying the national average yield for the commodity times the higher of: (1) the season-average market price and (2) the loan rate for the commodity.

If the actual national revenue is below the national target revenue, the calculated payment per acre would be converted to a payment rate for producers by dividing the national revenue payment per acre by the U.S. average PCCP payment yield per base acre (Table 3). The total payment to a producer would equal the national average payment rate for the commodity times the producer's base acres times the producer's 2002 PCCP program payment yield times 85 percent. RCCP target yields and corresponding revenue targets for program commodities are shown in Table 4.

Since the House bill gives producers the one time option to choose between the current price-based CCP and the new revenue-based CCP, producers must determine which option is best for their operation. Based on preliminary analysis, determining which option is optimal is not clear-cut. It will depend on producers' expectations of future prices, risk preferences, acreage bases, and CCP payment yields.

Table 3. Example Calculations of House Revenue-Based Counter-Cyclical (RCCP) Program for Corn.

	Corn Scenario #1 Actual Price=\$2.00/bu. Actual Yield=170.0/bu.	Corn Scenario #2 Actual Price=\$2.30/bu. Actual Yield=130.0/ac.
Target Price	\$2.63/bu.	\$2.63/bu.
Direct Payment	\$0.28/bu.	\$0.28/bu.
Effective Target Price	\$2.35/bu.	\$2.35/bu.
Olympic Avg Yield (2002-06)	146.4 bu./ac.	146.4 bu./ac.
Target Revenue (a)	\$344.12	\$344.12
Actual Revenue (b)	\$340.00	\$299.00
Payment Per Acre (a-b)	\$4.12	\$45.12
Program Yield (c)	114.4 bu./ac.	114.4 bu./ac.
Payment Rate Per Bushel (a-b / c)	\$0.036	\$0.394

Table 4. RCCP Target Yields and Revenues.

	Target Yield (unit/ac)	Target Revenue (\$/acre)
Corn (bu)	146.4	\$344.12
Sorghum (bu)	59.1	\$131.28
Barley (bu)	61.6	\$153.30
Oats (bu)	62.4	\$92.10
Wheat (bu)	41.3	\$149.92
Soybeans (bu)	41.0	\$231.87
Minor oilseeds (lb)	1207.3	\$129.18
Rice (cwt)	67.3	\$548.06
Upland cotton (lb)	784.7	\$496.93
Peanuts (ton)	1.38	\$683.83

Table 5 compares how the PCCP and RCCP programs would have performed over the last thirty years based on actual market prices and trend-adjusted yields. For all four crops considered, the PCCP triggered payments more often, but sorghum was the only crop in which the average PCCP payment was significantly larger than the RCCP payment. Corn was the only crop that had larger average RCCP payments. The RCCP triggered payments less frequently, but payments were often larger than PCCP payments when they were triggered. Higher average expected payments may not be the only criteria for selecting the optimal program. It is conceivable that one program may result in lower payments on average, but provide improved risk protection.

Table 5. Comparison of PCCP and RCCP Options for Kansas Crops based on Trend-Adjusted Yields and Market Prices (1977-2006).

Comparison Measure	Wheat	Corn	Soybeans	Sorghum
PCCP Avg Payment (\$/ac)	\$9.92	\$13.75	\$3.03	\$5.68
PCCP Frequency of Payment	73.3%	50.0%	33.3%	53.3%
PCCP Avg Paid Payment (\$/ac)	\$13.52	\$27.51	\$9.09	\$10.65
RCCP Avg Payment (\$/ac)	\$9.50	\$15.50	\$2.76	\$1.94
RCCP Frequency of Payment	70.0%	46.7%	30.0%	23.3%
RCCP Avg Paid Payment (\$/ac)	\$13.57	\$33.21	\$9.21	\$8.30

Payment Limitations

Payment limitation provisions are another change in the Commodity Title of the House bill. Notably, the House bill eliminates the three-entity rule in which producers can effectively double the individual payment limit by receiving full payments under one business entity and payments up to half the individual limit in up to two additional entities. The House bill also modifies the current payment limit caps for each commodity program. The direct payment limit changes from \$40,000 (\$80,000 under three-entity rule provisions) to \$60,000. The counter-cyclical payment limit is \$65,000, which equals the individual limit for counter-cyclical payments from the 2002 Farm Bill, but is \$65,000 less than the limit allowed under three-entity rule provisions. Marketing loan benefits, including loan deficiency payments and marketing loan gains have no limitations under the House bill. In the 2002 Farm Bill, marketing loan benefits were limited to \$75,000 per person per year (\$150,000 under three-entity rule provisions). However, forfeitures of commodities under loan to the government or repayments of loans with generic certificates were available and not subject to the payment limit.

By eliminating the three-entity rule, the House bill will require direct attribution of payments to the individuals who will receive them. With direct attribution, producers will be able to be involved in as many entities as they choose, but payments from those entities cannot total more than the individual limits for direct and counter-cyclical payments. However, spouses in farming operations receiving payments will also be eligible to receive payments—effectively doubling the individual limits for the farm operation.

In addition to the individual payments limits, the House bill reduces the adjusted gross income (AGI) eligibility standard. The 2002 Farm Bill established commodity program eligibility requirements based on AGI. Producers with AGI greater than \$2.5 million were not eligible for commodity payments unless 75 percent of that income came from agricultural sources. The House bill makes all producers with AGI greater than \$1 million ineligible for commodity and conservation payments. Producers with AGI between \$500,000 and \$1 million are eligible for these payments if two-thirds of income is earned from farming or farming related investments.

Conservation Programs

The 2002 Farm Bill was arguably the most conservation oriented farm bill in history. Broad support for conservation programs among agricultural and non-agricultural groups presents the likelihood that conservation programs will remain an important part of the 2007 Farm Bill. The House bill largely extends conservation programs that were in place in the 2002 Farm Bill. Priorities for additional funding focused on the Environmental Quality Incentives Program (EQIP), the Grassland Reserve Program (GRP), and the Farm and Ranchland Protection Program (FRPP). The conservation program receiving the largest increase in funding is EQIP, with an additional \$1.1 billion. As with the 2002 Farm Bill, 60 percent of EQIP funds will be allocated to livestock production.

The Conservation Reserve Program (CRP) is extended throughout the life of the bill at an authorized level of 39.2 million acres. A new CRP provision would allow retired landowners participating in CRP to modify their contracts to allow beginning or socially disadvantaged farmers the opportunity to return some of the land to grazing or crop production.

The Conservation Security Program (CSP), a working lands program that provides payments to farmers who use farming practices that benefit soil, water, and air resources, was implemented on a limited basis over the life of the 2002 Farm Bill. Though originally designed to be implemented nationwide, contracts were limited to select watersheds as funding was cut from the program to provide disaster assistance to farmers. Little additional funding for CSP was provided in the House bill, meaning that no new contracts will be awarded until 2012. However, some modifications for the existing program were made. The House bill eliminates the current three tiered system with an annual enhancement payment to pay producers for continuing existing conservation practices and implementing new ones. In addition, the modification of existing contracts will be permitted for current CSP participants.

Producers participating in conservation programs will be subject to some changes in payment limitations. Producers participating in one conservation program will be limited to \$60,000 per person—the same as the direct payment limit, while those participating in more than one conservation program will be subject to a limitation of \$125,000.

Energy Programs

The 2002 Farm Bill was the first farm bill that included an energy title. Leading up to debate in the U.S. House of Representatives, energy—much like conservation, was expected to be a hallmark of the 2007 Farm Bill. Overall, enhancements to the energy title are expected to cost \$2.4 billion over baseline funding. The most significant changes in the title include a program that provides up to \$2 billion in loan guarantees for biorefineries and biofuels production plants. Another program, the Feedstock Flexibility Program would subsidize the use of sugar for ethanol production. Aside from these programs, the energy title primarily continues, in many cases with increased funding, programs established in the 2002 Farm Bill.

Miscellaneous Programs

A new title to the House version of the 2007 Farm Bill is the Horticulture and Organic Title. This is noteworthy in that fruits, vegetables, and other specialty crops are poised to receive significant funding for the first time in U.S. farm bill history. Although the funding for specialty crops is not in the form of direct subsidies it is nevertheless designed to support the industry in several ways. First, the specialty crop block grant program was provided \$365 million in mandatory funding. In this program, block grants are provided to states to support projects in research, marketing, education, pest and disease management, production, and food safety. Previously, this program relied on annual appropriations from Congress. Increased funding was also provided to USDA for the purchase of fruits, vegetables, and nuts for use in domestic nutrition and food assistance programs. Mandatory funding was also provided for pest and disease detection and control for fruits and vegetables.

A provision in the Miscellaneous Title of the House bill is also noteworthy. Provisions for the implementation of mandatory Country of Origin Labeling (COOL) for meat were agreed to. The COOL provisions in the House bill establish three labeling options for meat. These options include: 1) U.S. Country of Origin label for animals born, raised, and slaughtered in the U.S., 2) Mixed Origin meat label for animals that were not exclusively born, raised, and slaughtered in the U.S., and 3) Imported Meat label for animals from foreign countries. These provisions also allow for ground meat products to be labeled with a list of countries from which the products could be derived. Verification of country of origin can be provided through existing business records, animal health papers, import or customs documents, or producer affidavits. In addition, some of the penalties for non-compliance with COOL provisions were reduced.

2007 FARM BILL COMMODITY TITLE ALTERNATIVES IN THE SENATE

Although the Senate Agriculture Committee has not yet gone through the process of marking up a bill for consideration by the committee or the entire Senate, some bills have been introduced which indicate some of the different approaches the Senate could take in developing the new farm bill. Many calls have been made to reform farm subsidies. In the House, a reform movement was led by Rep. Ron Kind (D-WI) and Rep. Jeff Flake (R-AZ). They were lead co-sponsors of FARM21, legislation that was designed to significantly change U.S. farm policy. Renamed as “Fairness in Farm and Food Policy”, this legislation was offered as an amendment to House Agriculture Committee bill, but was defeated by a large margin. However, a similar bill was introduced by Senator Richard Lugar (R-IN).

Lugar Food and Agriculture Risk Management for the 21st Century (FARM21) Act

FARM21 would make some fairly dramatic changes to current commodity programs. In this proposal, direct payments would continue, but would be reduced over the life of the farm bill. In addition, recipients would be required to place an increasing portion of those payments in newly created farmer-held income stabilization accounts. These accounts

would essentially be savings accounts in which farmers would be able to make withdrawals when sales fall below 95% of a farmer's five-year rolling average. Current counter-cyclical payments would be retained, while the marketing loan program would be replaced by a recourse loan program. In addition, the milk income loss contract (MILC) would be replaced with dairy income stabilization accounts, and the sugar program would be eliminated. The estimated savings from these changes in commodity programs would fund expanded nutrition, rural development, conservation, and renewable energy programs.

Durbin-Brown Farm Safety Net Improvement Act of 2007

Another bill that would make some significant changes in commodity programs was introduced by Senators Richard Durbin (D-IL) and Sherrod Brown (D-OH). Referred to as the Farm Safety Net Improvement Act of 2007, the Durbin-Brown bill would eliminate the current price-based counter-cyclical and marketing loan programs in favor of a new revenue-based counter-cyclical program (RCCP). The proposed revenue program would guarantee revenue at the state level (90% of 27-year state trend yield x expected national price). If actual revenue (actual state yield x national price at harvest) is less than the target revenue, then a payment of 90% of the difference between the guarantee and actual revenue would be made. Since the RCCP would be integrated with crop insurance, any payment made under the RCCP would be subtracted from any individual crop insurance indemnity payment.

This program would differ from the RCCP in the House bill on several points. First, revenue is guaranteed on a state basis, not a national basis as in the House bill. Second, payments under the Durbin-Brown bill are tied to actual planted acres, not base acres. Third, revenue guarantees under the Durbin-Brown bill are based on current market prices, not pre-determined, fixed target prices. Finally, any revenue payments under the Durbin-Brown bill are directly integrated with crop insurance payments. The integration with crop insurance would require current individual and group policies to be re-rated, which would likely result in lower premium costs.

USDA Farm Bill Proposals

A third direction the Senate could take would be to implement some portion of the 2007 Farm Bill proposal from USDA. In late January, USDA released their farm bill proposals which essentially maintained the basic structure of the current three-part safety net. The most significant change recommended by USDA was to convert the current price-based counter-cyclical program to a revenue-based counter-cyclical program. The House bill adopted the USDA revenue proposal in giving the producers the option to choose between the price and revenue programs. Beyond that recommendation, USDA also proposed some adjustments in the basic rates of the marketing loan and direct payment programs as shown in Table 6.

Table 6. USDA Farm Bill Proposals for Marketing Loan Rates and Direct Payments.

Commodity	Loan Rates			Direct Payment Rates		
	Current	Average of Proposed Rates, 2008-2012	Proposed Maximum	Current	Proposed 2008-09, 2013-17	Proposed 2010-2012
Corn (bu)	\$1.95	\$1.89	\$1.89	\$0.28	\$0.28	\$0.30
Sorghum (bu)	\$1.95	\$1.89	\$1.89	\$0.35	\$0.35	\$0.37
Barley (bu)	\$1.85	\$1.70	\$1.70	\$0.24	\$0.25	\$0.26
Oats (bu)	\$1.33	\$1.21	\$1.21	\$0.02	\$0.02	\$0.03
Wheat (bu)	\$2.75	\$2.58	\$2.58	\$0.52	\$0.52	\$0.56
Soybeans (bu)	\$5.00	\$4.92	\$4.92	\$0.44	\$0.47	\$0.50
Minor oilseeds (lb)	\$0.0930	\$0.0870	\$0.0870	\$0.0080	\$0.0080	\$0.00857
Rice (cwt)	\$6.50	\$6.50	\$6.50	\$2.35	\$2.35	\$2.52
Upland cotton (lb)	\$0.5200	\$0.4570	\$0.5192	\$0.0667	\$0.1108	\$0.1108
Peanuts (ton)	\$355.00	\$336.00	\$336.00	\$36.00	\$36.00	\$38.61

Regarding marketing loans, USDA proposed to establish the marketing loan rate for all program crops at 85 percent of the five-year Olympic average market price, subject to a maximum loan rate as established in the House version of the 2002 Farm Bill. The change in maximum rates would mean lower loan rates for most commodities, particularly upland cotton. USDA also proposed direct payments that are predominantly in keeping with the existing direct payment rates for the first two years of the new farm bill before increasing slightly over the last three years of a presumed five-year farm bill before reverting to the former rates at the end of the next farm bill.

USDA also proposes some modifications in the mechanics of the current safety net programs. Most significantly, the posted county price for loan repayment would shift from a daily calculation to a monthly calculation and the posted county price for purposes of the loan deficiency payment would apply to the day beneficial interest is lost, removing the flexibility to establish the LDP or loan repayment rate separately from the time of cash marketing.

Other proposals relevant to commodity programs include elimination of the restriction on planting fruits and vegetables on commodity program base acres, changes in payment limitation and program eligibility rules. USDA's proposed farm bill recommendations would attribute payments directly to individuals, eliminate the three-entity rule, and make modifications to the overall payment limits for each part of the program. More significantly, USDA proposed a change in the program eligibility rules for adjusted gross income (AGI). The proposed rules would lower the AGI cap from \$2.5 million to \$200,000 and would eliminate the 75 percent farm income exclusion.

SUMMARY

Progress on the 2007 Farm Bill has increased significantly in recent months, but a lot of work remains to be done. The Bush Administration and the U.S. House of Representatives have each put forth their proposals. Although the Senate has yet to markup legislation, signals have been given on the content of the Senate version of the

farm bill. Indications are that the Senate bill will include aspects of the current commodity program safety net like direct payments and some type of revenue counter-cyclical program. While it is unlikely that funding for commodity programs will be greatly reduced, it is also unlikely that funding will be increased. Spending is likely to be increased for conservation, energy, and nutrition programs, however. A potential battle between the House and Senate may develop in how to allocate conservation funds. Another potential battle between the House and the Senate may develop around the payment limitation issue, as support for tighter payment limitations may be greater in the Senate. Finding sufficient offsets to fund the higher spending in the Senate bill will be a challenge, as it was in the House. It may be difficult to pass a farm bill before the current law expires on September 30, but it appears both Houses of Congress and the Bush Administration would like to pass legislation this year. Although the final shape of the 2007 Farm Bill is still uncertain, it is certain that the debate on the bill will continue to be interesting.