Farm Commodity Programs in the 2008 Farm Bill

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Summary

Farm commodity price and income support provisions in the Food, Conservation, and Energy Act of 2008 (P.L. 110-246, the 2008 farm bill) include three primary types of payments:

- Direct payments unrelated to production or prices;
- Counter-cyclical payments for a commodity that are triggered when

  (a) prices are below statutorily-determined target prices, or
  (b) revenue falls below a historical guaranteed level; and

- Marketing assistance loans that offer interim financing and, if prices fall below loan prices set in statute, additional income support.

The farm commodity programs are the most visible part of the farm bill. In recent years, five crops (corn, wheat, cotton, rice, and soybeans) account for over 90% of government commodity payments to farmers.

The 2008 farm bill generally continues the farm commodity price and income support framework of the 2002 farm bill, with modifications. It continues the direct payment, counter-cyclical payment, and marketing loan programs for the 2008-2012 crop years, but adjusts target prices and loan rates for some commodities. The law also creates a pilot revenue-based counter-cyclical program ("ACRE") beginning with the 2009 crop year. The new law also has a pilot program for planting flexibility, new restrictions on base acres developed for residential use, and elimination of benefits to farms with fewer than 10 acres of program crops. For the 2008 crop year, the programs are essentially unchanged from the 2002 farm bill.

Payment limits both determine eligibility and set a maximum amount of commodity payments per person. The 2008 farm bill revises payment limitations for the commodity programs by tightening some limits and relaxing others. Limits are tightened by (1) reducing the adjusted gross income (AGI) limit to $500,000 of non-farm AGI and $750,000 of farm AGI, (2) eliminating the "three-entity rule," which allowed individuals to double their payments by having multiple ownership interests (doubling by having a spouse continues), and (3) requiring "direct attribution" of payments to a living person. Limits are relaxed by eliminating any limit on the marketing loan program. The new rules do not take effect until the 2009 crop year.

Implementation has been problematic in two ways. First, the Administration did not allow farmers to combine land before enforcing the 10-acre restriction, an allowance Congress mentioned only in report language. Consequently, Congress passed H.R. 6849 to suspend enforcement of the 10-acre provision for one year and offset the cost with reductions in computer technology outlays and changes to the new permanent disaster program. The bill awaits the President's signature.

The second implementation issue is that USDA is considering using prices from crop years 2006 and 2007 for setting the 2009 ACRE revenue guarantee, rather than the immediate past two years of 2007 and 2008, as Congress intended. The regulations, however, have not yet been released.

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Introduction

On June 18, 2008, the Food, Conservation, and Energy Act of 2008 (P.L. 110-246, the2008 farm bill) became law when the House and Senate voted to override President Bush's veto of H.R. 6124.[1] The U.S. Department of Agriculture (USDA) has begun the process of implementing the new law.

This report describes the farm commodity programs in the 2008 farm bill for the major crops such as wheat, corn, cotton, rice and soybeans. It also discusses the important policy developments in the new law compared to prior law.

For more details on the legislative history of the farm bill and a side-by-side summary of its provisions and changes, see CRS Report RL34696, *The 2008 Farm Bill: Major Provisions and Legislative Action*, by Renée Johnson et al.

Background

Economics Shape Perceptions of Farm Subsidies

The economic argument for the farm commodity price and income support programs is that markets do not efficiently balance commodity supply with demand. Imbalances develop because consumers do not respond to price changes by buying proportionally smaller or larger quantities (food demand is price inelastic). Similarly, farmers do not respond to price changes by proportionally reducing or increasing production (supply is price inelastic). These imbalances may contribute to volatile farm income, which can result in inadequate (or exaggerated) resource adjustments by farmers. Moreover, the long time lag between planting and harvest may magnify imbalances because economic and yield conditions may change.

The economic argument against the farm commodity programs is that, like any subsidy, the farm programs distort production, capitalize benefits to the owners of the resources, encourage concentration of production, and comparatively harm smaller domestic producers and farmers in lower-income foreign nations.

The objectives of federal commodity programs are to stabilize and support farm incomes by shifting some of the risks to the federal government. These risks include short-term market price instability and longer-term capacity adjustments. The goals are to maintain the economic health of the nation's farm sector so that it can utilize its comparative advantages to be globally competitive in producing food and fiber.

[1] The conference agreement on the 2008 farm bill was originally approved by the House and the Senate as H.R. 2419 and vetoed by the President in May 2008. Both chambers overrode the veto, making the bill law (P.L. 110-234). However, the trade title was inadvertently excluded from the enrolled bill. To remedy the situation, both chambers repassed the farm bill conference agreement (including the trade title) as H.R. 6124. The President vetoed the measure in June 2008 and both chambers again overrode the veto, which made H.R. 6124law as P.L. 110-246, and superseded P.L. 110-234.

Federal law mandates support for a specific list of farm commodities. For most of these commodities, support began during 1930s Depression-era efforts to raise farm household income when commodity prices were low because of prolonged weak consumer demand. While initially intended to be a temporary effort, the commodity support programs survived, but have been modified away from supply control and management of commodity stocks into direct income support payments.

Critics of commodity programs usually acknowledge the underlying economic conditions that make stability more difficult to achieve for agriculture than for some other sectors. However, they argue that (1) current programs are highly distorting of world production and trade, (2) the levels of subsidies are high and have become capitalized into land prices and rents that raise the cost of production and make the United States less competitive in global markets,[2] and (3) the benefits are concentrated among a comparatively small number of commodities produced on a small number of large farms.[3]

When farm programs were first authorized in the 1930s, most of the 6 million farms in the United States were small and diversified. Policymakers reasoned that stabilizing farm incomes using price supports and supply controls would help a large part of the economy (25% of the population lived on farms) and assure abundant food supplies. In recent decades, the face of farming has changed. Farmers now comprise less than 2% of the population. Most agricultural production is concentrated in fewer, larger, and more specialized operations. About 8% of farms account for 75% of farm sales (these 175,000 farms had average sales over $1 million). Most of the country's 2 million farms are part-time, and many operators rely on off-farm jobs for most of their income.

Supporters of commodity subsidy programs may not contradict the critics, but do point out that other nations have distorting subsidy programs and/or trade barriers that should be eliminated if the United States is to make reforms. Landowners are concerned about a loss of rents and wealth if land prices drop in response to a reduction in the subsidies. Similarly, rural communities are concerned about any large decline in the real estate tax base that supports local schools, roads, and other community services. While large farms receive most of the production-linked subsidy payments, recipients argue that lower input costs and marketing efficiencies make large farms efficient and small farms uneconomic in the production of bulk commodities. Therefore, targeting subsidies to small farms, recipients say, would encourage inefficient production.

Authorizing Legislation

The authority for USDA to operate farm commodity programs comes from three permanent laws, as amended: the Agricultural Adjustment Act of 1938 (P.L. 75-430), the Agricultural Act of 1949 (P.L. 81-439), and the Commodity Credit Corporation (CCC) Charter Act of 1948 (P.L. 80-806). Congress typically alters these laws through multi-year omnibus farm bills to address current market conditions, budget constraints, or other concerns.

[2] Predictable government payments are capitalized into land values and rents. Since 60% of program acres are rented, the landowners receive many benefits (M. Burfisher and J. Hopkins, "Farm Payments," *Amber Waves*, USDA Economic Research Service, Feb. 2003).

[3] J. MacDonald, R. Hoppe, and D. Banker, "Growing Farm Size and the Distribution of Commodity Program Payments," *Amber Waves*, USDA Economic Research Service, Feb. 2005.

If a new farm bill is not enacted when an old one expires, we would revert to the permanent laws mentioned above for the commodities programs. Under permanent law, eligible commodities would be supported at levels much higher than they are now, and many of the currently supported commodities might not be eligible. Since reverting to permanent law is incompatible with current national economic objectives, global trading rules, and federal budgetary policies, pressure builds at the end of one farm bill to enact another.[4]

The 2008 farm bill (P.L. 110-246) contains the most recent version of the commodity price and income support programs. It supersedes the commodity programs of previous farm bills, and suspends the relevant price support provisions of permanent law.

Eligible Commodities

Federal support exists for about two dozen farm commodities representing nearly one-third of gross farm sales. Five crops (corn, cotton, wheat, rice, and soybeans) account for about 90% of these payments. About 66% of the payments go to 10% of recipients.

- The **"covered commodities"** are the primary crops eligible for support: **wheat, corn, grain sorghum, barley, oats, upland cotton, rice, pulse crops (dry peas, lentils, small chickpeas, and large chickpeas), soybeans, and other oilseeds (including sunflower seed, rapeseed, canola, safflower, flaxseed, mustard seed, crambe, and sesame seed*)*. Peanuts** are supported similarly. Farmers receive constant "direct payments" tied to historical production (except pulse crops do not receive direct payments despite being a covered commodity). Farmers may also receive "counter-cyclical" and "marketing loan" payments that increase when market prices (or, in some cases, revenue) are low.
- **"Loan commodities"** include **all of the "covered commodities" plus extra long staple cotton, wool, mohair**, and **honey**. These commodities are eligible for the marketing loan program only.
- **Dairy** prices are indirectly supported through federal purchases of nonfat dry milk, butter, and cheese. Producers also receive a counter-cyclical "milk income loss contract" (MILC) payment when prices fall below a target price. See CRS Report RL34036, *Dairy Policy and the 2008 Farm Bill*, by Ralph M. Chite.
- **Sugar** support is indirect through import quotas and domestic marketing allotments. No direct payments are made to growers and processors. See CRS Report RL34103, *Sugar Policy and the 2008 Farm Bill*, by Remy Jurenas.

Meats, poultry, fruits, vegetables, nuts, hay, and nursery products (about two-thirds of farm sales) do not receive direct support or payments in the commodity title of the farm bill.

Eligible Producers

The 2008 farm bill defines a producer (for purposes of farm program benefits) as an owner-operator, landlord, tenant, or sharecropper that shares in the risk of producing a crop and is

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[4] For more background on the consequences of reverting to permanent law, see CRS Report RL34154, *Possible Expiration (or Extension) of the 2002 Farm Bill*, by Jim Monke et al.

entitled to a share of the crop produced on the farm. In addition, an individual must comply with certain conservation and planting flexibility rules. A term commonly used in federal regulations is "actively engaged in farming," which generally means providing significant contributions of capital (land or equipment) and labor and/or management, and receiving a share of the crop as compensation. Conservation rules include protecting wetlands, preventing erosion, and controlling weeds. Planting flexibility rules allow crops other than the program crop to be grown, but generally prohibit planting fruits or vegetables on subsidized acreage.

Modern farming enterprises usually involve some combination of owned and rented land. Two types of rental arrangements are common: cash rent and share rent.

- Under cash rental contracts, the tenant pays a fixed cash rent to the landlord. The landlord receives the same rent, bears no risk in production, and thus is not eligible to receive program payments. The tenant bears all of the risk, takes all of the harvest, and receives all of the government subsidy.
- Under share rental contracts, the tenant usually supplies most of the labor and machinery, while the landlord supplies land and perhaps some machinery or management. Both the landlord and tenant bear risk in producing a crop and receive a portion of the harvest.[5] Both are eligible to share in the government subsidy.

Even though tenants might receive all of the government payments under cash rent arrangements, they might not keep all of the benefits if landlords demand higher rent. Economists widely agree that a large portion of government farm payments passes through to landlords, and that government payments raise the price of land. About 60% of acres enrolled in the government commodity programs are rented.[6]

Farm Commodity Program Provisions

The farm commodity price and income support provisions in the 2008 farm bill include three primary types of payments:

- **Direct payments** unrelated to production or prices;
- **Counter-cyclical payments** which are triggered when

  (a) prices are below statutorily-determined target prices, or
  (b) revenue for a commodity falls below a historical guaranteed level, and

- **Marketing assistance loans** that offer interim financing and, if prices fall below loan prices set in statute, additional income support, sometimes paid as **loan deficiency payments (LDP)**.

[5] For example, a typical share rental arrangement in some regions is a 50-50 split of the crop harvested, with the landlord supplying all of the land and half of the cost of certain inputs such as fertilizer. The tenant supplies all of the labor and pays the remaining share of the input costs. Management decisions, such as crop diversification, are usually made jointly.

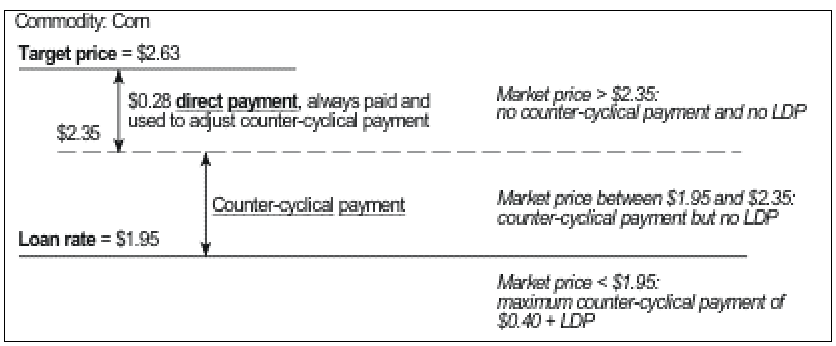
[6] M. Burfisher and J. Hopkins, "Farm Payments," *Amber Waves*, USDA Economic Research Service, Feb. 2003.

The first two types of payments are subject to payment limits on the size of payments. All three types of payments may be subject to income eligibility limits, depending on the size of farm and non-farm income.

The 2008 farm bill generally continues the farm commodity price and income support framework of the 2002 farm bill, with modifications. It continues the direct payment, counter-cyclical payment, and marketing loan programs for the 2008-2012 crop years, but adjusts target prices and loan rates for some commodities. The law also creates a pilot revenue-based counter-cyclical program ("ACRE") beginning with the 2009 crop year. It revises payment limitations by tightening some limits and relaxing others. The new law also has a pilot program for planting flexibility, new restrictions on base acres developed for residential use, and elimination of benefits to farms with fewer than 10 acres of program crops. For the 2008 crop year, the programs are essentially unchanged from the 2002 farm bill.

Figure 1 illustrates the three types of commodity payments in relation to market prices. Of the counter-cyclical payments, only traditional price-triggered counter-cyclical payments are included in the figure. Using corn as an example, if market prices are above $2.35/bushel, neither counter-cyclical nor marketing loan benefits (e.g., LDP) would apply. If market prices are between $1.95 and $2.35/bushel, a counter-cyclical payment would accrue, but no LDP would be available. If market prices are below the loan rate of $1.95/bushel, the maximum counter-cyclical payment of $0.40/bushel is made, and an LDP would be available equal to the difference between the $1.95 loan rate and the market price. Regardless of market prices, however, the direct payment of $0.28/bushel is paid.

Figure 1. Relationship of Commodity Payments to Market Prices



Source: CRS

An important consideration for the farm commodity programs is how they are classified for trade purposes. As a member of the World Trade Organization (WTO), the United States made agricultural policy commitments under the WTO's Agreement on Agriculture. All WTO members agree to submit annual notifications of their farm program outlays to the WTO, and these outlays are subject to specific limits. For the United States, its total spending limit for programs that are considered to be trade distorting is $19.1 billion per year. Other types of payments are not subject to limits if they are "decoupled" or not considered to be trade distorting.

Direct Payments

Direct payments (DP) are fixed annual payments based on historical production; they do *not* vary with current market prices or yields. Recent high commodity prices and high farm incomes have made it difficult for some to justify the annual outlays for direct payments, which amount to $5 billion per year. Eligible commodities include wheat, corn, grain sorghum, barley, oats, upland cotton, rice, peanuts, soybeans, and other oilseeds (including sunflower seed, rapeseed, canola, safflower, flaxseed, mustard seed, crambe, and sesame seed).

A farm is eligible for direct payments in proportion to its "base acres" (which are a constant historical average of its planting history of a particular commodity). For many farms, base acres date to the 1980s, but for some farms base acres were updated in 2002. In addition to its base acreage, each farm has a "direct payment yield" for each commodity, which is also an unchanging historical average based on the farm's actual yields over the 1981-1985 period.

A farmer is not obligated to grow the covered commodity to receive a direct payment for that commodity (e.g., a farm may plant soybeans on corn base acres, and receive the direct payment for corn). The rationale for this planting flexibility is to allow farmers to respond to market signals when choosing crops.

Because direct payments are constant and allow planting flexibility, they are arguably less distorting of production than prior farm programs that had greater government intervention.[7] Direct payments thus are thus known as "decoupled" payments, and the United States has classified them as "green box" when reporting agricultural subsidies to the WTO. Green box payments help countries comply with international trade agreements because they do not count against subsidy ceilings.[8]

However, because the planting flexibility rules still have restrictions on planting fruits and vegetables (discussed later in this report), the direct payment program may be subject to challenge as to whether it qualifies as a green box payment.[9] This challenge was raised during the 2008 farm bill debate as a reason to revise the direct payment program or allow complete planting flexibility, but the program was not changed.

In the 2008 farm bill, the direct payment rates per commodity remain the same as in the 2002 farm bill (**Table 1**), but the overall formula to compute the payment contains a 2% reduction in direct payments for crop years 2009-2011. Conferees accomplished this by changing the ratio of base acres on which direct payments are made from 85% to 83.3%.[10] The 85% ratio is restored for the 2012 crop year to maintain a higher baseline for the next farm bill.

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[7] Before planting flexibility was introduced in the early 1990s, farmers were required to grow the commodity for which they had base acres in order to participate in the government program. To control production when surpluses existed, the government often required farmers to "set aside," or not plant, part of their base acreage.

[8] For a brief discussion about WTO procedures for classifying government support programs, see CRS Report RS20840, *Agriculture in the WTO: Limits on Domestic Support*, by Randy Schnepf.

[9] In 2007, Canada and Brazil initiated WTO cases against the U.S. farm programs, charging that direct payments are inappropriately classified in the green box. See CRS Report RL34351, *Brazil's and Canada's WTO Cases Against U.S. Agricultural Support*, by Randy Schnepf.

[10] The reduction in payment acres to 83.3% does not affect the counter-cyclical payment formula, but the lower percentage is used for planted acreage in the ACRE program.

Table 1. Support Prices for Farm Commodities in the 2008 Farm Bill

Type of payment	Direct payment rate			Counter-cyclical target price					Marketing loan rate				
Law or proposal	2002 farm bill	2008 farm bill	Change from 2002 farm bill	2002 farm bill	2008 farm bill			Change from 2002 farm bill	2002 farm bill	2008 farm bill			Change from 2002 farm bill
					Crop year					Crop year			
					2008	2009	2010-2012			2008	2009	2010-2012	
Wheat, $/bu	0.52	0.52	+0	3.92	3.92	3.92	4.17	+0.25	2.75	2.75	2.75	2.94	+0.19
Corn, $/bu	0.28	0.28	+0	2.63	2.63	2.63	2.63	+0	1.95	1.95	1.95	1.95	+0
Sorghum, $/bu	0.35	0.35	+0	2.57	2.57	2.57	2.63	+0.06	1.95	1.95	1.95	1.95	+0
Barley, $/bu	0.24	0.24	+0	2.24	2.24	2.24	2.63	+0.39	1.85	1.85	1.85	1.95	+0.10
Oats, $/bu	0.024	0.024	+0	1.44	1.44	1.44	1.79	+0.35	1.33	1.33	1.33	1.39	+0.06
Upland Cotton, $/lb	0.0667	0.0667	+0	0.724	0.7125	0.7125	0.7125	-0.0115	0.52	0.52	0.52	0.52	+0
Rice, $/cwt	2.35	2.35	+0	10.50	10.50	10.50	10.50	+0	6.50	6.50	6.50	6.50	+0
Soybeans, $/bu	0.44	0.44	+0	5.80	5.80	5.80	6.00	+0.20	5.00	5.00	5.00	5.00	+0
Minor oilseeds, $/lb	0.008	0.008	+0	0.101	0.101	0.101	0.1268	+.0258	0.093	0.093	0.093	0.1009	+0.0079
Peanuts, $/ton	36	36	+0	495	495	495	495	+0	355	355	355	355	+0
Peas, dry, $/cwt				na	na	8.32	8.32	na	6.22	6.22	5.40	5.40	-0.82
Lentils, $/cwt				na	na	12.81	12.81	na	11.72	11.72	11.28	11.28	-0.44
Sm.chickpeas, $/cwt		not applicable		na	na	10.36	10.36	na	7.43	7.43	7.43	7.43	+0
Lg.chickpeas, $/cwt				na	na	12.81	12.81	na	na	na	11.28	11.28	na

Type of payment	Direct payment rate			Counter-cyclical target price					Marketing loan rate				
Law or proposal	2002 farm bill	2008 farm bill	Change from 2002 farm bill	2002 farm bill	2008 farm bill, Crop year: 2008	2008 farm bill, Crop year: 2009	2008 farm bill, Crop year: 2010-2012	Change from 2002 farm bill	2002 farm bill	2008 farm bill, Crop year: 2008	2008 farm bill, Crop year: 2009	2008 farm bill, Crop year: 2010-2012	Change from 2002 farm bill
ELS cotton, $/lb									0.7977	0.7977	0.7977	0.7977	+0
Wool, graded, $/lb									1.00	1.00	1.00	1.15	+0.15
Wool, nongraded									0.40	0.40	0.40	0.40	+0
Mohair $/lb	not applicable			not applicable					4.20	4.20	4.20	4.20	+0
Honey, $/lb									0.60	0.60	0.60	0.69	+0.09
Sugar, raw cane, $/lb									0.18	0.18	0.1825	(2010)0.1850 (11-12) 0.1875	+0.0075
Sugar, beet, $/lb									0.229	0.229	128.5% of loan rate for cane		+0.0119

Source: CRS.

The law eliminates advance direct payments beginning in the 2012 crop year. This delays advance payment of 22% of the direct payment from the December before most crops are planted to the following October at or after harvest, and thus into a new fiscal year.[11] This scores budget savings of about $1.1 billion in FY2012. Although farmers will have to wait longer, they will receive their full payment.

Participants in the new ACRE counter-cyclical program will continue to receive direct payments, but their direct payment amount will be reduced by 20% as required by the 2008 farm bill.

Counter-Cyclical Payments

The traditional counter-cyclical payment (CCP) program makes automatic payments when market prices fall below target prices set in statute.[12] Historically, the farm commodity programs have focused on price, but producers have cited insufficient government support during years with natural disasters when yields are low and prices are high. In those years, they have little to sell and thus do not benefit from high market prices, but do not receive counter-cyclical support either. In response to this criticism, the 2008 farm bill creates a revenue-based counter-cyclical program called the Average Crop Revenue Election (ACRE). The ACRE program is an alternative to the traditional price counter-cyclical program, and is based on statewide crop-specific revenue data. ACRE makes payments when actual revenues from a commodity are less than a market-based, moving average revenue guarantee.

Eligible commodities for either counter-cyclical option include the covered commodities for the direct payment program (wheat, corn, grain sorghum, barley, oats, upland cotton, rice, peanuts, soybeans, and other oilseeds), plus four new pulse crops beginning in 2009 (dry peas, lentils, small chickpeas, and large chickpeas).

Traditional Counter-Cyclical Payments (CCP)

Traditional counter-cyclical payments compensate for the difference between a crop's target price and a lower effective market price.[13] When effective market prices exceed the target price, no payment is made.

As with direct payments, traditional counter-cyclical payments are proportional to a farm's base acres and "counter-cyclical payment yield," and do not depend on current production. Although the counter-cyclical program payment rate formula depends on market prices, it does not require

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[11] For example, without the provision eliminating advance payments, an advance direct payment for crop year 2012 would have been paid in December 2011 (FY2012). With advance payments eliminated, farmers will need to wait until October 2012 (FY2013). This pattern continues thereafter, rolling advance direct payment amounts into later fiscal years.

[12] This type of price support was first implemented in 1973 as the "deficiency payment," but was discontinued in the 1996 farm bill. The 2002 farm bill reinstated counter-cyclical payments for wheat, feed grains, rice, and upland cotton and extended them to soybeans, other oilseeds, and peanuts. Dairy also has a direct counter-cyclical payment created in 2002—the milk income loss contract (MILC)—but with a different payment mechanism.

[13] The effective price is the higher of (a) the national season-average market price or (b) the national loan rate, plus the direct payment rate. By adding the direct payment rate, the formula recognizes that farmers receive direct payments and avoids paying them more than the target price. The CCP compensates for lower market prices down to the loan rate, below which the marketing loan program supports.

the farmer to produce any of the commodity. Thus it is partially decoupled; it is decoupled from yield and acreage, but not from market prices. The United States has classified them as "amber box" when reporting agricultural subsidies to the WTO, and thus they are limited in size together with other amber box subsidies.

The 2008 farm bill continues the traditional price counter-cyclical program, although it adjusts target prices and adds new commodities (**Table 1**). Six out of 10 ongoing commodities receive a target price increase (wheat, sorghum, barley, oats, soybeans, and minor oilseeds), one has a small decrease (cotton), three are unchanged (corn, rice, and peanuts), and four are new in 2009 (dry peas, lentils, small chickpeas, and large chickpeas).

Some commodity groups argued that their support levels were not high enough relative to other commodities in the 2002 farm bill (e.g., wheat and soybeans).

The decrease in the cotton target price is the only change in the 2008 crop year. The new crops are added in the 2009 crop year. None of the target price increases occur until the 2010 crop year.

The 2008 farm bill generally makes counter-cyclical payments after the October 1 that falls after the end of the marketing year[14] and eliminates advance counter-cyclical payments beginning with the 2011 crop year, both of which help score budget savings by delaying some payments compared to the 2002 farm bill.

Participants in ACRE are ineligible for traditional counter-cyclical payments.

Average Crop Revenue Election (ACRE)

Beginning with the 2009 crop year, farmers may choose either the traditional CCP or the new revenue-based ACRE option. Participants in ACRE will continue to receive direct payments, but at a 20% reduced rate. Participants will also continue to be eligible for nonrecourse marketing loans, but with a 30% lower loan rate. Producers who choose ACRE (whether in 2009, 2010, 2011, or 2012) may not revert to the traditional CCP for the remainder of the farm bill. The ACRE program is available for the same crops as traditional counter-cyclical payments, but is based on planted acres rather than base acres.[15]

If market prices are expected to be high, ACRE might be preferred by many farmers because the traditional counter-cyclical payments would be zero or small. Even under high prices, ACRE may help farmers manage downside systemic risks—that is, manage the risks that are inherent in the market and cannot be diversified away. And, as market price falls, ACRE may make payments when traditional counter-cyclical programs would not. ACRE is expected to perform better than traditional counter-cyclical programs under high-price environments, in states with larger yield increase since the 1980s, in states with more variable yields, and in states that are outside the primary growing regions of a particular commodity.[16]

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[14] A "marketing year" is the 12-month period after a commodity is harvested. A "crop year" refers to the calendar year in which a commodity is harvested. For example, corn harvested in the fall of 2008 is in the 2008 crop year. The marketing year for the 2008 crop of corn begins in October 2008 and continues until September 2009.

[15] The total number of planted acres enrolled in ACRE cannot exceed the total number of base acres for all covered commodities on a farm.

[16] Carl Zulauf, "Understanding ACRE: Breakeven Price With Traditional Programs, Corn Soybeans, Wheat," The Ohio (continued...)

To receive an ACRE payment, two triggers need to be met:

- First, the actual state revenue for a supported crop during the crop year must be less than the state-level revenue guarantee amount.
- Second, an individual farm's actual revenue for a supported crop must be less than the farm's benchmark revenue.

The second trigger keeps farms from receiving payments when they did not have a sufficient loss, even if the state as a whole sustained a loss in revenue for the crop.

The state-level revenue guarantee amount and the individual farm benchmark revenue are determined by the product of a guaranteed price with a guaranteed level of production. Benchmark or guaranteed yields at the state and farm levels are Olympic averages of the most recent five years.[17] Price guarantees are averages of the higher of (a) the marketing year price or (b) the marketing loan rate as reduced under ACRE for the most recent two years. The revenue guarantee is 90% of the product of the average benchmark yield and the price guarantee. The 10% reduction allows for some variation in revenue before subsidy payments begin (similar to a deductible). Changes in the revenue guarantee are limited to plus or minus 10% from the previous year.

If both triggers are met, an individual farm will receive an ACRE payment that is based on the state-level difference between actual revenue and the ACRE guarantee per acre, multiplied by a percentage (83.3% in crop years 2009-2011, or 85% in crop year 2012) of the farm's planted acreage, but pro-rated based on the individual farm's yield history compared to the state's yield history. The maximum payment rate is 25% of the ACRE guarantee.

ACRE is modeled largely on the Average Crop Revenue (ACR) proposal in the Senate-passed version of the farm bill (H.R. 2419), but is significantly modified.[18] The House-passed farm bill (H.R. 2419) offered a pilot revenue counter-cyclical program based on national-level revenues. The state-level plan will make payments more often than a national-level plan since a smaller area is more likely to fall below average production than a larger area.

Because the revenue guarantee is a moving average and year-to-year changes are limited, the guarantee will lag changes in the market. If the market price declines over several years, this may lead to higher outlays than traditional CCP as the adjustment to the lower price level occurs.[19]

(...continued)

State University, Department of Agricultural, Environmental, and Development Economics, AEDE-RP-0109-08, June 2008, 1 p., [http://aede.osu.edu/resources/docs/pdf/wegfsz4y-ag7a-vxx7-j003psoreuml1a3f.pdf].

[17] Olympic averages are averages computed after deleting the highest and lowest observations. Thus, an Olympic average over a five year period is an average of three data points, after deleting the highest and lowest observations during the five-year period.

[18] Compared to the Senate bill, the ACRE program starts a year earlier (in 2009), and has less change to its interaction with direct payments and marketing loans. The Senate bill would have replaced direct payments with a $15/acre "fixed payment" and offered only recourse loans.

[19] Carl Zulauf, "Understanding ACRE: Its Revenue Guarantee," The Ohio State University, Department of Agricultural, Environmental, and Development Economics, AEDE-RP-0110-08, June 2008, 1 p., [http://aede.osu.edu/resources/docs/pdf/5rrj4kax-12oh-nkfa-5ygy8jaj56vom7ng.pdf].

USDA Concerns and Implementation Issues

The Administration has criticized the ACRE program because its two-year price guarantee feature will incorporate the historically high recent market prices into the guarantee, and consequently allow possibly large payments to farmers if market prices decline from their currently record high levels.[20] The Administration has argued that the Congressional Budget Office (CBO) score of this program, for purposes of estimating budgetary impacts of the legislation, does not reflect the magnitude of this possibility because market prices in the baseline are expected to remain high.[21]

In light of these concerns over the level of outlays, the Administration has indicated that it may not use the immediately preceding two crop years to set the revenue guarantee level for ACRE, as instructed in statute. This has caused debate between Congress and the Administration over congressional intent. The Administration wants to use prices from 2006 and 2007 when implementing ACRE for the 2009 crop year. This would set a lower revenue guarantee, and keep federal outlays lower. Members in Congress say the farm bill requires using prices from 2007 and 2008 for ACRE in 2009, and that those are the years that were used by CBO when scoring the farm bill. Because the Administration has not yet released regulations for the ACRE program, the final disposition of this dispute is not yet determined.

Marketing Loans and Loan Deficiency Payments

Marketing loans are nonrecourse loans[22] that farmers can obtain by pledging their harvested commodities as collateral. Traditionally, the loans provide interim financing by allowing farmers to receive some revenue for their crop when the loan is requested, while at the same time storing the commodity for later disposition when prices may be higher.[23] As an alternative to taking out a loan, the loan deficiency payment (LDP) is a cash payment option that allows farmers to sell grain in response to market signals without putting their commodity under loan, while receiving the price benefits of the loan program.

Marketing loans provide minimum price guarantees on the crop actually produced, unlike direct or counter-cyclical payments, which are tied to historical bases. They are *not* decoupled as they depend both on current production and market prices. The United States has classified them as "amber box" when reporting agricultural subsidies to the WTO.

[20] USDA, "Press Conference with Deputy Secretary of Agriculture Chuck Conner on the Presidential Veto of the Farm Bill," May 21, 2008, at [http://www.usda.gov/wps/portal/!ut/p/_s.7_0_A/7_0_1OB?contentidonly=true&contentid=2008/05/0134.xml].

[21] Dan Morgan, "Farm Bill's Subsidy Costs May Rise; Billions More Could Be Paid Through Little-Noticed Provision," *Washington Post*, May 21, 2008, p. A02.

[22] "Nonrecourse" means that the collateral can be forfeited at the end of the term with no penalty. The government takes no recourse against the borrower beyond accepting the commodity as full settlement of the loan, even if the market price of the commodity is less than the loan.

[23] The marketing loan program allows farmers to pay creditors with money from the USDA loan and not make marketing decisions based on the immediate need to pay creditors. Without the loan program, farmers sometimes would need to sell their crop at low harvest prices to pay operating expenses, and not be able to benefit from a cyclical rise in market prices. Market prices of covered commodities within a marketing year usually follow a predictable pattern. They are often lowest at harvest when a surge of new supply floods the market, and grain not stored on the farm is delivered to elevators. As the marketing year progresses, prices gradually rise to compensate for storing the commodity and to draw the commodity out of storage in response to new demand.

National-level loan prices are set by the farm bill (**Table 1**), and are negotiated in the legislative process, rather than established based on formulas using historical market prices as was done in farm bills before 1990. USDA adjusts the national average loan rate to local (usually county) loan rates to reflect spatial difference in markets and transportation.[24]

Commodities eligible for marketing loans include all of the commodities that are eligible for direct and counter-cyclical payments, plus extra long staple (ELS) cotton, wool, mohair, and honey. However, ELS cotton is not eligible for loan deficiency payments. Sugar receives assistance through commodity loans, but under a separate provision with unrelated procedures.

The 2008 farm bill continues the nonrecourse marketing loan program under the same framework as in the previous farm bill (**Table 1**). The 2008 farm bill increases the loan rate for eight out of 20 commodities (wheat, barley, oats, minor oilseeds, graded wool, honey, cane sugar, beet sugar), decreases the loan rate for two commodities (dry peas, lentils), and adds one new pulse crop beginning with the 2009 crop year (large chickpeas).

Loan rates for the 2008 crop year are the same as under the 2002 farm bill. Increases in loan rates do not occur until the 2010 crop year, while changes for the pulse crops occur in the 2009 crop year.

Participants in the ACRE counter-cyclical program continue to be eligible for marketing loans and LDPs, but loan rates will be reduced by 30% as required in the farm bill.

Beneficial Interest

Beneficial interest generally refers to owning the commodity or having a stake in its disposition. Beneficial interest is lost when the commodity is sold. The Administration had recommended that the farm bill change the "beneficial interest" rule,[25] but Congress did not change it. The rule allows farmers to lock in their LDP when market prices are low (usually at harvest), continue to own the commodity, and sell it at a future and possibly higher market price than when the LDP was determined. Policy makers said they wanted farmers to continue to have the flexibility to market their commodities in response to market signals and benefit from the program.

Advocates for change pointed out that if farmers can sell their crop for more than the support price, then government support should be unnecessary. More generally, if farmers can sell their crop for more than the market price at the time that the LDP was determined, the LDP would not need to be as large. These advocates for change wanted the determination of the LDP to be tied to when a farmer loses beneficial interest.

Although the beneficial interest rules remain the same, the loan repayment rate (also known as the posted county price, or PCP) used to determine the LDP is to be computed using a 30-day average of market prices, rather than the daily repayment rate of the 2002 and prior farm bills. Using a 30-day average for the repayment rates will lessen, but not eliminate, the market timing strategies that some farmers have used to maximize LDPs.

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[24] Local loan prices are available at [http://www.fsa.usda.gov/FSA/webapp?area=home&subject=prsu&topic=lor].

[25] USDA 2007 farm bill proposal, p. 22, at [http://www.usda.gov/documents/fbcommodity_071.pdf].

Cotton Users Payment

Among the special marketing loan provisions for upland cotton (which continue the prior law policies of special import quotas and limited global import quotas), the 2008 farm bill also creates a new payment for domestic users of upland cotton. The payment is termed "economic adjustment assistance," and is only to be used to acquire, construct, modernize, develop, convert, or expand operations. Unlike the Step 2 cotton payment that was eliminated following a WTO ruling against the U.S. cotton program,[26] the new cotton users payment is for upland cotton of domestic or foreign origin. The payment is 4 cents per pound from August 1, 2008, to July 31, 2012. Thereafter, the payment rate is 3 cents per pound.

Payment Limits

Two types of payment limits exist for the farm commodity programs. One sets the maximum amount of farm program payments that a person can receive per year. The other sets the maximum amount of income that an individual can earn and still remain eligible for program benefits (a means test). The farm commodity programs have had the first type of limit since 1970. The means test was added starting with the 2002 farm bill, and also is known as the adjusted gross income (AGI) limit.

The 2008 farm bill makes several changes to payment limits, some by tightening the limits and others by relaxing them.

- Limits are tightened by

  (a) reducing the AGI limit,

  (b) eliminating the "three-entity rule," which allowed individuals to double their payments by having multiple ownership interests, and

  (c) requiring "direct attribution" of payments to a living person instead of to a corporation, general partnership, etc.

- Limits are relaxed by eliminating any limit on marketing loans.

The new payment limit rules do not take effect until the 2009 crop year.

Factors Affecting Payment Limits

The payment limits issue is controversial because it directly addresses questions about what size farms should be supported, whether payments should be proportional to production or limited per individual, and who should receive payments. The effect of payment limits varies across regions. The South and West have more large farms than the Upper Midwest or Northeast, and are more affected by payment limits. Cotton and rice farms are affected more often than corn, soybean, or wheat farms since the former group's subsidies per acre are higher.

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[26] For more information about the Step 2 program and the WTO ruling, see CRS Report RL32571, *Brazil's WTO Case Against the U.S. Cotton Program*, by Randy Schnepf.

Supporters of payment limits use both economic and political arguments to justify tighter limits. Economically, they contend that large payments facilitate consolidation of farms into larger units, raise the price of land, and put smaller, family-sized farming operations at a disadvantage. Even though tighter limits would not redistribute benefits to smaller farms, they say that tighter limits could help indirectly by reducing incentives to expand, and could help small and beginning farmers buy and rent land. Politically, they believe that large payments undermine public support for farm subsidies and are costly. Newspapers have published stories critical of farm payments and how they are distributed to large farms, non-farmers, or landowners.[27] Limits are increasingly appealing to urban lawmakers, and have advocates among smaller farms and social interest groups.

Critics of payment limits (and thus supporters of higher limits or no limits) counter that all farms are in need of support, especially when market prices decline, and that larger farms should not be penalized for the economies of size and efficiencies they have achieved. They say that farm payments help U.S. agriculture compete in global markets, and that income testing is at odds with federal farm policies directed toward improving U.S. agriculture and its competitiveness.

Limits on the Size of Payments

Under the 2008 farm bill, the annual limit on payments that are directly attributed to a person is $105,000 for direct and counter-cyclical payments combined. The payment limit has two parts: $40,000 for direct payments, and $65,000 for counter-cyclical payments. These amounts effectively can be doubled to a combined $210,000 for a sole proprietor's farm by having a spouse (**Table 2**). These amounts are the same as in the 2002 farm bill.

Corporations, partnerships, and trusts are eligible for payments, but the payments must be attributed to a living person by the fourth level of ownership. Payments for most commodities are combined toward a single limit, but a separate and equal payment limit applies to peanuts.

Marketing loan gains and LDPs are unlimited in the 2008 farm bill, a change from prior law that had imposed a $75,000 limit but that could be avoided legally by using commodity certificates to repay marketing loans.[28] Both the House- and Senate-passed bills chose to eliminate limits on marketing loans altogether in the 2008 farm bill, rather than apply payment limits to the use of commodity certificates. This was in response to concerns from cotton and rice growers who did not want tighter limits, and who were already opposing reductions in the AGI limit. Since commodity certificates now are viewed by many as unnecessary, the farm bill terminates authority to use certificates to repay marketing loans after the 2009 crop year.

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[27] For example, see the *Washington Post* series "Harvesting Cash," published in 2006, at [http://www.washingtonpost.com/wp-srv/nation/interactives/farmaid/].

[28] Marketing loan benefits in the 2002 farm bill were essentially unlimited because producers could use commodity certificates without limit when other marketing loan options were limited. Cotton and, to a lesser extent, rice farms were the primary users of certificates. Corn, soybeans, and wheat used certificates minimally. The prior law allowed certificates (7 U.S.C. 7286), and farmers essentially bought certificates at a discount and used them to repay their loans. But, technically, a certificate exchange was a momentary forfeiture, followed by "in-kind" receipt of commodities in exchange for a certificate bought at a discounted price, and only available to marketing loan participants (USDA, Report of the Commission on the Application of Payment Limitations for Agriculture, Aug. 2003, pp. 80-83, at [http://www.usda.gov/oce/reports/payment_limits/paymentLimitsAll.pdf].

Table 2. Commodity Payment Limit Provisions in the 2008 Farm Bill

Type of Limit	Prior Law	2008 Farm Bill		
	2002 Farm Bill	**House-passed H.R. 2419**	**Senate-passed H.R. 2419**	**Enacted P.L. 110-246**
Adjusted Gross Income (AGI) Limitation				
Ineligible for payments if AGI exceeds...	$2.5 million, unless 75% from farming	$500,000, unless 67% from farming $1 million, firm (no exceptions)	2008: $2.5 m[a] 2009: $1.0 m[a] 2010: $750,000[a]	Non-farm AGI: $500,000 (all pmts.) Farm AGI: $750,000 (DP only)
Allocate AGI on joint return	No	No	Yes	Yes
Direct and Counter-Cyclical Payments (separate limit for peanuts)				
(a) Direct Payments	$40,000	$60,000	$40,000	$40,000[b]
(b) Counter-Cyclical, ACRE	$65,000	$65,000	$60,000	$65,000[b]
Doubling allowance	spouse, 3-entity	spouse	spouse	spouse
Subtotal, doubled	*$210,000*	*$250,000*	*$200,000*	*$210,000*
Marketing Loan Payments (separate limit for peanuts)				
(c1) Marketing Loan Gains (c2) Loan Deficiency Pmt.	$75,000			
(c3) Commodity Certificates (c4) Loan Forfeiture Gains	Unlimited	Unlimited	Unlimited	Unlimited
Subtotal (c1) (c2), doubled	*$150,000*			
Subtotal (c1) through (c4)	*Unlimited*			
Sum of Direct, Counter-Cyclical, and Marketing Loan Payments				
Total of limited payments	***$360,000*** *(a), (b), (c1), (c2)*	***$250,000*** *(a), (b)*	***$200,000*** *(a), (b)*	***$210,000*** ***(a), (b)***
Total including all payments	***Unlimited***	***Unlimited***	***Unlimited***	***Unlimited***

Source: CRS.

a. Unless 67% from farming.

b. For ACRE participants, the $40,000 direct payment limit is reduced by the amount of the 20% reduction in the individual's direct payment. The amount of the reduction is added to the $65,000 limit on counter-cyclical payments.

Because the 2008 farm bill eliminates any limit on marketing loans, it is difficult to compare the $210,000 limit of the 2008 farm bill with the $360,000 limit of the 2002 farm bill. The $360,000 limit was for three types of payments; the $210,000 limit is for only two types of payments.

Doubling the Limits

The 2008 farm bill continues the "spouse rule" that allows a husband and wife to be treated as separate persons to double a farm's payment limit. It repealed, however, the long-standing "three-entity rule," which allowed an alternative means of doubling by letting one person receive payments on up to three entities, with second and third entities being eligible for one-half of the limits (one whole plus two halves results in doubling).

For the AGI limit, the 2008 farm bill allows a married couple to divide their income for the AGI test as if separate income tax returns had been filed. This effectively allows doubling if the income is divided in an exact manner (discussed below).

Direct Attribution

When the three-entity rule was repealed, it was replaced with "direct attribution." Rather than tying payment limits to farm organization, which sometimes promoted the creation of entities for the purpose of doubling payment limits, the 2008 farm bill allows payments to various types of entities. But it now requires that the payments be attributed to a living person based on ownership shares in the entities. If a payment to a business entity cannot be allocated to a living person after four levels of ownership, the payment to the overall entity is reduced proportionately. Thus, individual people may receive payments on any number or ownership arrangement of farms (not limited to three entities), but the total amount of payments attributed to each living person may not exceed the statutory limits.

Adjusted Gross Income (AGI) Limits

The 2008 farm bill adopts a slightly different approach from the 2002 farm bill for the AGI limit. Formerly, the AGI limit had an exception if 75% of AGI was earned from farming sources. The 2008 farm bill eliminates the exception and creates two new measures of AGI: adjusted gross non-farm income, and adjusted gross farm income.

First, if a three-year average of non-farm AGI exceeds $500,000, then no program benefits are allowed (direct, counter-cyclical, and marketing loan). Second, if a three-year average of farm AGI exceeds $750,000, then no direct payments are allowed (but counter-cyclical and marketing loan benefits are allowed for these higher-income farmers). **Table 2** shows that program participants can have income from both sources, but the caps for each type are "hard" caps (that is, there are no exceptions to the cap as with "soft" caps, except that the cap on farm AGI applies only to direct payments).

For example, if a full-time farmer has non-farm AGI over $500,000, his/her program payments are eliminated regardless of his/her farm income. Another example is that a taxpayer may have AGI between $750,000 and $1.25 million and still receive program benefits if the income is split in such a way as to remain below the caps on farm and non-farm income.

Moreover, the 2008 farm bill adopts a Senate provision that allows the AGI of a married couple to be divided as if separate tax returns were filed. While this provision theoretically allows doubling of the AGI limits to $2.5 million for a married couple, the income needs to be legitimately allocated both between the spouses and by the types of income, likely by Social Security numbers or equivalent identifiers. Such doubling to $2.5 million would be more difficult than the $2.5 million AGI test of the 2002 farm bill.

How Many Farmers Are Affected?

Reliable national data on the effect of payment limits are rare, especially for the payment limit or AGI levels specified in the 2008 farm bill. However, data developed since enactment of the 2002 farm bill provide some guidance on the general magnitude of the effects.

According to the report of the Payment Limits Commission mandated by the 2002 farm bill,[29] about 1% of producers receiving payments in 2000 were affected by the $40,000 limit on what now are called direct payments. This amounted to 12,300 producers across 42 states. The reduction was $83 million, or 1.6% of the value of payments, with California and Texas accounting for 36% of the reduction.

Under the 2002 farm bill's AGI limit of $2.5 million, annual data suggest that only about 3,100 (0.15%) farmers had AGI over $2.5 million. Since not all of these farm taxpayers receive commodity subsidy payments and some likely would have qualified for the 75% farm income exception, USDA estimated that the 2002 farm bill's AGI cap affected only a few hundred farmers.[30]

Masked by these data is the fact that limits could be avoided, usually legally, by reorganizing a farm.[31] In fact, one study in 2007 suggests that about 20% of rice farmers reorganized their business because of limits, despite only 1.2% appearing to be subject to the limit.[32] The 2008 farm bill's elimination of the three-entity rule and application of direct attribution to living persons should lessen reorganization of farm businesses solely for purposes of avoiding payment limits.

In terms of the 2008 farm bill, data are not yet available that are specific to the farm bill limits of $500,000 non-farm AGI and $750,000 farm AGI. During the debate over tighter limits, USDA data suggested that about 1.5% of farm operator households have AGI over $200,000 and received some farm program payments (1.1% of farm sole proprietorships, 2.5% of farm partnerships, and 9.7% of farm households involved in farming through a corporation). About 8.5% of rice farms and 9.3% of cotton farms have AGI over $200,000 and receive program payments. This compares to 5.5% for corn farms and only 1.3% for soybean farms.[33]

The farms potentially affected by the AGI limit are not necessarily large farms, nor necessarily above the AGI limit because of high *farm* income. Supporters of the AGI proposal say farmers are skilled at managing income taxes and can keep taxable farm income lower using tax incentives and rules.[34] The portion of farmers affected by the relatively higher limits in the farm bill would be smaller than the percentages in the preceding paragraph.

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[29] USDA, Payment Limit Commission Report, pp. 65-75.

[30] Ron Durst, *Effects of Reducing the Income Cap on Eligibility for Farm Program Payments*, USDA-ERS Report EIB-27, Sept. 2007, [http://www.ers.usda.gov/publications/eib27/eib27.pdf].

[31] USDA, pp. 31-39; and GAO, *Farm Program Payments: USDA Needs to Strengthen Regulations and Oversight to Better Ensure Recipients Do Not Circumvent Payment Limitations*, GAO-04-407, April 2004, pp. 20-26, at [http://www.gao.gov/new.items/d04407.pdf].

[32] Barrett Kirwan (University of Maryland) "The Distribution of U.S. Agricultural Subsidies," May 2007, p. 19-22, at [http://www.aei.org/docLib/20070515_kirwanfinal.pdf].

[33] Ron Durst, USDA-ERS, at [http://www.ers.usda.gov/publications/eib27/eib27.pdf].

[34] AGI is a common measure of household taxable income, and combines income from all sources. AGI measures net income, and Schedule F farm income contributes to AGI on a net basis, that is, after farm business expenses. Farms overwhelmingly report losses for tax purposes (because of cash accounting, depreciation, and other practices), even though USDA farm income numbers are positive. For example, in 2004, two-thirds of all Schedule F tax returns showed a loss, resulting in a sector-wide net farm *loss* of $13 billion for all Schedule F returns. By comparison, USDA farm income data showed an $80 billion *profit*. Even for "large" farms with sales over $250,000, about one-third report a loss for tax purposes. Source: CRS analysis of IRS data at [http://www.irs.gov/taxstats/index.html], and USDA-ERS, *Effects of Federal Tax Policy on Agriculture*, by Ron Durst and James Monke, AER 800, April 2001, at [http://www.ers.usda.gov/publications/aer800/aer800.pdf].

Other Attempts to Change Payment Limits

Besides the changes in payment limits agreed to by conferees and enacted in the 2008 farm bill, there have been five votes specifically or predominately focused on payment limits since 2002 (four in the Senate and one in the House). All of these amendments advocated further tightening of the limits. None resulted in the amendments being successfully enacted into law. However, three received a majority vote in the Senate, but they were either deleted during conference negotiations (as in the 2002 farm bill), or did not meet procedural hurdles requiring a 60-vote majority to avoid a filibuster (as in the 2008 farm bill).

The Administration also proposed a major tightening of payment limits in its 2007 proposal for the farm bill.[35] The Administration's plan for a $200,000 AGI cap colored the debate about payment limits throughout the 2008 farm bill's development. It became a lower limit of the range of possibilities (or a goal for some) when legislative compromises were proposed.

Other bills to revise payment limits have been introduced by Senators Dorgan and Grassley during each Congress since 2002, but did not receive action. They did, however, became the foundation for the various Dorgan/Grassley floor amendments that are described below which did receive votes. Senator Klobuchar also proposed a tighter AGI limit in the Senate that received a floor vote. Representative Kind included payment limits as a major part of his floor amendment that was a substitute for the commodity title. Payment limit proposals receiving floor votes since 2002 and the Administration's 2007 plan are summarized blow.

- **Grassley/Dorgan amendment to the 2008 Senate farm bill.** An amendment by Senators Grassley and Dorgan (S.Amdt. 3695 to H.R. 2419) to lower the limit on payments from $360,000 to $250,000 and apply the limits to all marketing loan options received a 56-43 vote. Despite having a majority, it did not receive the 60 votes necessary to avoid a filibuster.
- **Klobuchar amendment to the 2008 Senate farm bill.** An amendment by Senator Klobuchar (S.Amdt. 3810 to H.R. 2419) to tighten the AGI limit to $250,000 unless more than 67% of AGI is farm income, and $750,000 with no exceptions, received a 48-47 vote. Despite receiving a majority, it did not have the 60 votes necessary to avoid a filibuster.
- **Kind Amendment to the House 2007 farm bill.** An amendment by Representative Kind (H.Amdt. 700 to H.R. 2419) to generally revise the commodity programs, including tightening payment limits, failed by a vote of 117-309. The amendment would have tightened the AGI limit to a firm $250,000 cap for everyone and $125,000 unless 66% of AGI came from farming.
- **USDA's 2007 farm bill proposal.** The Administration's 2007 farm bill proposal would have denied payments to households with more than $200,000 of AGI, with no exception, redistributed the $360,000 limit across the payment types, and eliminated the three-entity rule. It was not incorporated in its entirety into any legislation.
- **Budget reconciliation in 2005.** When Congress debated farm bill changes as part of budget reconciliation in 2005, a floor amendment by Senator Grassley to

[35] USDA 2007 farm bill proposal, pp. 36-55.

tighten payment limits failed by a procedural vote of 46-53 (S.Amdt. 2359 to S. 1932, 109th Congress).

- **Dorgan amendment to the 2002 farm bill.** The Senate-passed version of the 2002 farm bill contained tighter limits (S.Amdt. 2826 to S. 1731, 107th Congress). The vote was 66-31 in favor of tighter limits, but those limits were rejected by the conference committee.

Other Commodity Provisions

Eliminating Payments on Fewer than 10 Acres

The 2008 farm bill eliminates direct and counter-cyclical payments to farms with fewer than 10 base acres (combined across all crops). The exclusion, however, does not apply to farms owned by socially disadvantaged[36] or limited-resource farmers and ranchers. Moreover, Congress intended for farmers to be able to aggregate land across multiple farms they operate before USDA enforces the restriction.[37]

The justification for the prohibition on small payments and/or small farms is a desire by some to stop payments to non-farmers. Some landowners with small holdings receive payments but are not full-time farmers; they receive most of their income from non-farm jobs and are sometimes called hobby farmers. Supporters of the 10-acre restriction do not want to include these farmers as program beneficiaries. However, the restriction does not address payments to the non-farm landowners of larger farms who may still qualify for payments. Moreover, implementing the new provision may reduce the number of recipients (and the constituency) of the farm programs and increase the size of the average payment, which may have negative connotations.

Policy differences have arisen over congressional intent to allow farmers to combine parcels of land they farm before the 10-acre rule is enforced and the Administration's more restrictive interpretation of statute. The statute says:

> A producer on a farm may not receive ... payments if the sum of the base acres of the farm is 10 acres or less ... [but this provision] shall not apply to a farm owned by ... a socially disadvantaged farmer or rancher ... or a limited resource farmer or rancher. (P.L. 110-246, sec. 1101(d))

Strictly speaking, the statute does not mention aggregating or combining acreage. USDA chose to apply a direct interpretation of statute and does not give any weight to the conference report language that states:

> The Managers intend for the Department to allow for aggregation of farms for purposes of determining the suspension of payments on farms with 10 base acres or less. The Managers expect for the Department to review farms in this category on an annual basis rather than

[36] Socially disadvantaged farmers are defined for other farm programs as women, African Americans, American Indians, Alaskan Natives, Hispanics, Asian Americans and Pacific Islanders.

[37] The 2008 farm bill also requires USDA to track the use of land affected by the 10-acre requirement and issue a report on the impact on specialty crop producers. Some believe that more acres may go into production of fruits and vegetables if small acreages are disqualified from direct payments. Existing fruit and vegetable growers are wary of more acres competing with their specialty crops.

> prohibiting payments to these farms for the life of the farm bill. (H.Rept. 110-627 for H.R. 2419, pp. 674-675).

The Administration's regulation to implement this provision for the 2008 crop year has caused some farmers or landowners to be denied participation in the commodity programs. USDA adopted a strict interpretation of the statute and its regulations prohibited reconstitutions of farms under 10 acres unless the tracts were under the same ownership:

> [T]o be assured that producers on farms with base acres of 10 acres or less are prohibited from receiving payments ... [FSA] will not approve requests for farm combination reconstitutions of farms having base acres of 10 acres or less ... However, as an exception to the above rule, a farm with a total of 10 base acres or less may combine with another farm if one of the farms undergoes a change in land ownership [and the ownership of the two farms is identical]."[38]

Constituents have complained to Congress, and Members have written to USDA to say that USDA is not following congressional intent as explained in report language. Because of this implementation issue, both the House and Senate passed a bill, H.R. 6849, to suspend enforcement of the 10-acre requirement for the 2008 crop year. A longer-term fix is being left to the 111th Congress.

H.R. 6849 passed both the Senate and the House by unanimous consent on September 29, 2008. The bill now awaits the President's signature. Specifically, the bill:

- Suspends the 10-acre requirement for the 2008 crop year. Farms with less than 10 acres would be able to receive payments as they have in prior years.
- Extends the enrollment period for the commodity program for the 2008 crop year beyond the original deadline of September 30, 2008. Extending the sign-up period for farms under 10 acres allows those who were denied participation during the summer of 2008 by USDA regulations to still enroll and receive benefits. The extension will go until the later of November 14, 2008, or 45 days after enactment.
- Offsets the $9 million cost to suspend the provision for one year by:

  Reducing mandatory funds provided in the 2008 farm bill for information technology upgrades that support the crop insurance program. Originally, $15 million per year was to be available for FY2008-FY2011 ($60 million in total); H.R. 6849 reduces the amount for FY2011 by $6 million.

  Making changes to the new permanent disaster program regarding (1) treating minor acreages and grazing land, and (2) establishing a minimum loss threshold that requires a physical loss of at least 10 percent of one crop on the farm to qualify for payments. The later change prevents payments due solely to price reductions. The changes are scored to save $3 million.

Given the higher offsets required to make a more permanent correction to the 10-acre provision (possibly as much as $90 million over 10 years, as described in the next section), both chambers

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[38] *Federal Register*, vol. 73, no. 126 (June 30, 2008), p. 36840, at [http://www.fsa.usda.gov/Internet/FSA_Federal_Notices/dcp.pdf].

amended the original bill to the less expensive approach of a two-year suspension, and ultimately only a one-year suspension. Members have indicated that a longer-term fix will need to be addressed in the next Congress.

Earlier Versions of H.R. 6849

The House Agriculture Committee reported an earlier version of H.R. 6849 on September 19, 2008. A similar bill, S. 3538, was introduced in the Senate on September 23, 2008. These versions were nearly identical in suspending the 10-acre provision for two years, but differed primarily in their source of budgetary offsets. The House offset the $20 million cost of the two-year suspension entirely with reductions to the information technology account for crop insurance.[39] The Senate bill did not have any offsets.

The version of H.R. 6849 *as introduced* would have put congressional intent for aggregating farms into the statute. It would have added a third exception to the 10-acre requirement (in addition to exceptions for socially disadvantaged and limited-resource farmers): farms that add up to more than 10 acres when combined with other farms operated by the same person.

When the 2008 farm bill was enacted, CBO estimated that the 10-acre restriction would save about $88 million over 10 years (FY2008-FY2017); this estimate was based on statutory language and not on report language. Because the approach in H.R. 6849 as introduced would greatly reduce the number of farms excluded by the 10-acre requirement, the savings would be much less—most likely nearly eliminating the $88 million 10-year savings.

Definitions of Farm, Reconstitution, and Aggregation

The effect of the 10-acre minimum requirement depends greatly on the definition of "farm" in USDA regulation and implementation practices. Farmers can "reconstitute" their farms into larger or smaller units based on various actions. Congress refers to aggregation in the report language for the 10-acre provision. How does the use of these terms affect the provision?

The definition of "farm" to administer the commodity programs is different from other statistical or perceived definitions of farms. This may impact the policy differences between congressional intent and USDA's interpretation of statute. Under Farm Service Agency (FSA) regulations, a "farm" is one or more tracts of land considered to be a separate operation. Land in a farm does not need to be contiguous; however, a "tract"—a smaller unit—is a parcel of contiguous land under the same ownership.[40] When multiple tracts are treated as one farm, the tracts must have the same operator and owner, except that tracts with different owners may be combined into one farm if all owners agree.[41] Thus, one producer may be operating several "farms" if he/she is renting land from several landlords, or has purchased land in several tracts. It may be more common to combine farms that are under cash rental arrangements (where the operator receives all of the government payments), and less common to combine farms that are under share rental

[39] CBO cost estimate of H.R. 6849, as reported by the House Agriculture Committee, Sept. 22, 2008, at [http://www.cbo.gov/ftpdocs/97xx/doc9788/hr6849.pdf].

[40] 7 CFR 718.2.

[41] 7 CFR 718.201.

arrangements (where the landlord has a management role and receives some of the government payment).

"Reconstitution" is the process of combining (or dividing) tracts or farms for purposes of the commodity programs . In general, FSA requires reconstitution when a farmer buys land and operates it; in this way the number if farms per operator is minimized. When a farmer adds land to an operation by rental arrangements, FSA may allow—but does not necessarily encourage—voluntary reconstitutions.[42]

"Aggregation" is a term not used by USDA; aggregation seems only to have been used by Congress in the report language for the 2008 farm bill. The intent of Congress seems to be that aggregation is either a synonym for reconstitution or another means of combining acreage without triggering a formal reconstitution. That is, it basically means the same thing as a reconstitution; but by not using the term "reconstitute," perhaps Congress is allowing USDA to create another means of combining farms for the single purpose of the 10-acre requirement without triggering a formal reconstitution.

Budgetary Impact and Number of Farms

The number of base acres affected by the provision are expected to be comparatively small. The CBO budget estimate for this provision, based on the statute only, shows a savings up to $9 million per year, for about $37 million in savings over five years and $88 million over 10 years. This is less than 0.1% of the expected outlays for the commodity title.[43]

The following data illustrate differences in the number of farms based on two definitions. The number of "farms" as defined by FSA for the 2002 farm bill included 1.9 million "farms" with base acres. Some of these farms must have been combined into single operations, because the same database revealed only 1.3 million "producers" on those farms.[44] Given the similarity of the 2002 and 2008 farm bills regarding base acreage, these numbers are unlikely to change very much.

Under the more commonly known definition of farm used for the agriculture census ($1,000 of agricultural sales), there are 2.1 million farms. Not all of these farms have base acres or receive government payments. Only 531,000 farms in the census statistic received non-conservation farm payments in 2002.

The 1.9 million farms with base acres in FSA's definition is much greater than the 531,000 farms in the census receiving government payments. This indicates aggregation of farms within FSA's database into actual operating farms. Of the 2.1 million census farms, 78,000 had harvested crop land of fewer than 10 acres.[45] Some of these farms may be unsubsidized farms growing fruits and

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[42] CFR 1412.403; FSA Handbook, "Farm Reconstitutions," 2-CM, paragraph 89, updated 8/14/08, at [http://www.fsa.usda.gov/Internet/FSA_File/2-cm.pdf].

[43] In addition, using the CBO estimate of $9 million savings in FY2009, and a conservative assumption that only direct payments are affected, a rough calculation using an average payment of $20/acre would imply 450,000 acres being affected. This would be about 0.17% of the total 269 million base acres.

[44] USDA Economic Research Service, *Economic Analysis of Base Acre and Payment Yield Designations Under the 2002 U.S. Farm Act*, ERR-12, September 2005, p. 12 at [http://www.ers.usda.gov/publications/err12/err12.pdf].

[45] USDA National Agricultural Statistics Service, *2002 Agriculture Census*, "Table 6, Government Payments and Commodity Credit Corporation Loans," and "Table 9, Land in Farms, Harvested Cropland, and Irrigated Land, by Size (continued...)

vegetables, thus giving credence to the hypothesis that few farms may be excluded if broader reconstitution is allowed for farms under 10 acres.

Planting Flexibility for Fruits and Vegetables for Processing

As described previously, under the direct payment program farmers may plant crops other than the program crop and still receive direct payments—this is known as planting flexibility. They are prohibited, however, from planting fruits, vegetables, and wild rice on program crop base acres. Limited exceptions have allowed growers with a history of planting fruits and vegetables to continue to do so, but direct and counter-cyclical payments were reduced acre-for-acre of fruits and vegetables.

The restriction on planting fruits and vegetables is a seemingly reasonable response to protect growers of unsubsidized fruits and vegetables who do not want competition from subsidized growers of program crops. The planting restriction on fruits and vegetables, however, jeopardizes the ability of the United States to classify direct payments as non-distorting, decoupled, or "green box" for WTO accounting. The WTO has determined that the restrictions are inconsistent with the rules of a minimally distorting subsidy.[46]

Another complication with the restriction on planting fruits and vegetables surfaced when soybeans became eligible for direct payments in the 2002 farm bill. This created a shortage of acres in some parts of the Midwest for growing fruits and vegetables for processing (canning and freezing). Some landlords stopped allowing fruits and vegetables to be grown in rotation in place of soybeans. Many growers and processors asked for flexibility to grow fruits and vegetables for processing on base acres without other penalties, in return for giving up payments on those acres while growing fruits and vegetables. Such proposals became known as "farm flex."

The 2008 farm bill creates a pilot planting flexibility program for fruits and vegetables for processing, while continuing the overall restriction on planting fruits and vegetables on base acreage. The pilot program begins in 2009, and allows farmers in seven Midwestern states to plant base acres in cucumbers, green peas, lima beans, pumpkins, snap beans, sweet corn, and tomatoes grown for processing. Their base acres are temporarily reduced for the year (resulting in lower direct and counter-cyclical payments), but restored for the next crop year. The states include Minnesota (34,000 acres), Wisconsin (9,000 acres), Michigan (9,000 acres), Illinois (9,000 acres), Indiana (9,000 acres), Ohio (4,000 acres), and Iowa (1,000 acres).

The 2008 farm bill continues the exceptions of prior law that allowed farms with a history of growing fruits and vegetables to plant them, but with a one-year reduction in direct and counter-cyclical payment acres. The pilot program is similar in that it reduces payments acres, but in the aggregate is in addition to the acreage allowed under the continuation of the exceptions.

The additional planting flexibility of the pilot program addresses the subset of concerns in the Midwest, but it does not address concerns over WTO compliance. Restrictions on planting fruits and vegetables remain on acreage outside the pilot program, and for all fresh fruits and vegetables. The Administration had proposed eliminating the fruit and vegetable planting

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(...continued)

of Farm," at [http://www.agcensus.usda.gov].

[46] CRS Report RL32571, *Brazil's WTO Case Against the U.S. Cotton Program*, by Randy Schnepf.

restriction completely. For more background, see CRS Report RL34019, *Eliminating the Planting Restrictions on Fruits and Vegetables in the Farm Commodity Programs*, by Renée Johnson and Jim Monke.

Eliminating Base Acres in Residential Development

The 2008 farm bill adopts a Senate provision that eliminates base acres on land that has been subdivided into multiple residential units or other non-farming uses. Prior farm bills have eliminated base acres only for land developed for nonagricultural commercial or industrial use.

This provision addresses the issue raised in media stories about the farm programs making payments to non-farmers or for land that is not in production. A *Washington Post* article in 2006 identified the practice of non-farm homeowners receiving farm commodity payments on what had become known as "cowboy starter kits," which were residential developments in Texas on land with rice base acres. Developments of houses had been built on several acres each, and the few acres that were not directly in the yard of the house retained their rice base acreage and still qualified for direct payments, even though there was no intention by the homeowners to farm or maintain the land for agriculture.[47]

Limiting Payments to Deceased Farmers' Estates

The 2008 farm bill requires USDA to reconcile the social security numbers of program recipients with a Social Security database twice a year. The purpose is to assure that program beneficiaries are alive, and that estates do not continue to qualify beyond a reasonable period. USDA must also issue regulations describing how long a deceased person's estate may continue to qualify for program benefits. Prior to 2008, a USDA regulation already specified a two-year period for estates to qualify, unless excepted individually by the Secretary (7 C.F.R. 1400.206).

The farm bill provision will require USDA to reissue and update the regulation, and presumably to increase enforcement. The provision was in response to a 2007 GAO report showing that some farm commodity programs continued to be paid to deceased farmers or their estates beyond the two-year regulation.[48]

Cost of the Commodity Title

Because spending on the farm commodity programs is a combination of fixed decoupled payments and market-driven counter-cyclical payments, outlays may be highly variable from year to year. **Figure 2** shows that, from 1981 to 2007, commodity program outlays (including dairy and sugar, but excluding disaster payments) have ranged from a low of $3.3 billion in 1981 to a high of $27 billion in 2000. The average over the period was $11.1 billion per year. From 1981-1990, the average annual outlay was $11.4 billion; from 1991-2002, the average was $10.6 billion, and from 2003 to 2007 (roughly the years of the 2002 farm bill), the average was $11.7

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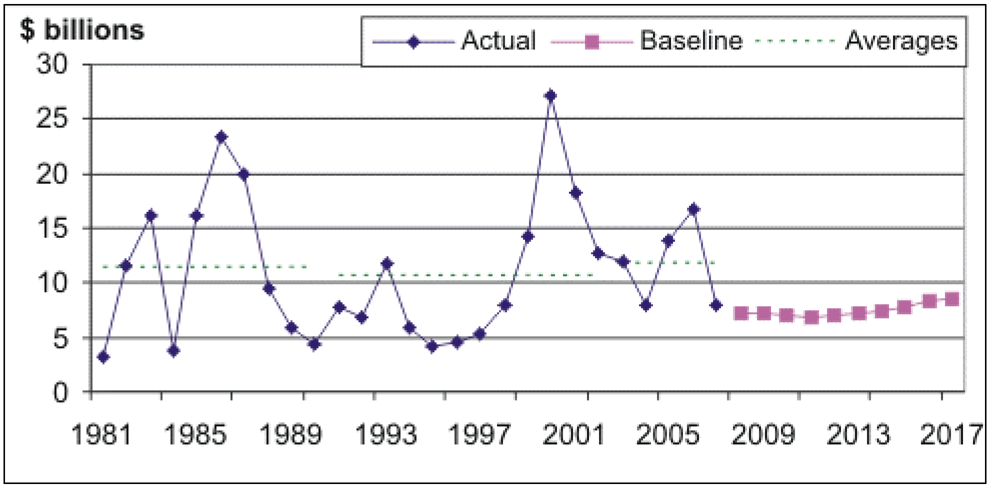
[47] *Washington Post*, "Farm Program Pays $1.3 Billion to People Who Don't Farm," July 2, 2006, A01 [http://www.washingtonpost.com/wp-dyn/content/article/2006/07/01/AR2006070100962.html].

[48] U.S. Government Accountability Office, *USDA Needs to Strengthen Controls to Prevent Improper Payments to Estates and Deceased Individuals*, GAO-07-818, July 2007 [http://www.gao.gov/new.items/d07818.pdf].

billion. The CBO forecast for the 2008-2017 period is about $7.4 billion annually, well below the historical averages due to the record high commodity prices at the time that the 2008 farm bill was enacted.

Figure 2. Farm Commodity Program Outlays



Source: CRS, using USDA "Table 35, CCC Net Outlays by Commodity and Function" and CBO baseline.

Compared to the baseline of continuing the provisions of the 2002 farm bill, the Congressional Budget Office (CBO) cost estimate (score) of the new provisions in Title I of the farm bill is a five-year savings of $1.726 billion and a 10-year savings of $1.658 billion. If the scores of these changes are added to the 2007 baseline of budget outlays used to write the farm bill, then CBO's expected cost of Title I is $41.628 billion for FY2008-2012 and $85.521 billion over 10 years (**Table 3**). This includes the program crop commodities, dairy, and sugar.

The 5- and 10-year savings that are scored for all of Title I are the net result of various provisions that both score savings or cost more than prior law. The largest savings is the result of a shift in the timing of direct payments. Making advance payments of a portion of direct payments is ended beginning with the 2012 crop year (**Table 3**). This shifts about $1.1 billion of payments into a later fiscal year, which achieves savings in the budget window but does not reduce the total amount eventually paid to farmers.

Other savings are scored by reducing the proportion of base acres on which direct payments are paid, reducing direct payments and marketing loan rates for participants in the new ACRE revenue counter-cyclical program, replacing some counter-cyclical payments with ACRE payments, eliminating advance counter-cyclical payments beginning in crop year 2011, and by tightening payment limits (**Table 3**).

Some of these savings are offset with costs of the new ACRE payments, economic assistance for cotton users, and higher target prices and loan rates for certain covered commodities, dairy, and sugar. CBO combines the effect of some of these provisions into a single score (e.g., raising counter-cyclical target prices and eliminating traditional counter-cyclical payments for ACRE participants). Thus, a provision-by-provision score is not possible.

Table 3. Cost of Provisions in Title I of the 2008 Farm Bill

(in millions of dollars)

Description	5 years: FY2008-FY2012	10 years: FY2008-FY2017
CBO baseline, March 2007, Title I	**43,354**	**87,179**
CBO score of changes in Title I of the 2008 farm bill		
Provisions with net savings:		
Direct payments (no advance pmt. for 2012 crop)[a]	-1,147	-1,147
Direct payments (2% cut; 20% reduction for ACRE)[a]	-792	-1,852
Counter-cyclical (target price, no advance, ACRE offset)	-614	-872
Payment limit changes	-258	-615
Marketing loan (adjust rates; 30% reduction for ACRE)	19	-550
No payments under 10 acres; planting flexibility	-45	-106
Provisions with net additional costs:		
ACRE (revenue payment component only)	182	2,015
Economic assistance for cotton users	337	616
Dairy	386	396
Sugar	69	231
Peanut and cotton storage and handling	82	166
Implementation costs	50	50
Storage facility loans	5	10
Subtotal: CBO Score of 2008 Farm Bill changes, Title I	**-1,726**	**-1,658**
CBO Estimate of Total Cost of Title I	**41,628**	**85,521**

Source: CRS, based on CBO baseline and score of the conference agreement of H.R. 2419.

a. CRS estimate of these two separate components in the combined CBO score.

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