Supplemental Income Payments: An Annual Farm Bill

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Introduction

During each of the past three years, low commodity prices and various weather problems have prompted Congress to pass legislation affording farmers supplemental income payments. At this writing, the House Agriculture Committee has voted to appropriate an additional $5.5 billion in supplemental payments for FY 2001. While the passage of annual farm legislation is not completely unprecedented, the levels and nature of the supplemental payments in 1998-2001 are truly a new occurrence.

Congress, of course, annually passes an Agricultural Appropriations Bill. In these bills and in recent so called "budget reconciliation" bills dealing with the budget deficit, Congress has on numerous occasions reduced farm program benefits, or denied or reduced funding to specific program features that were authorized in omnibus farm legislation. Congress has periodically enacted one-shot payments for natural disasters such as drought (1988, 1989) and flood (1993).

However, it has been rare for Congress to enact annual supplemental program payments for low prices. In part because of the supplemental payments, the level of spending and the dependence of the agricultural sector on the government over this four-year period are also unprecedented. In the year 2000, direct payments to farmers were estimated at $32.3 billion, compared to the previous record of $25.8 billion during the depths of the "Farm Crisis" in 1986. Government payments have averaged about 25 percent of net farm income during the past 20 years. In 1999, such payments were about one-half of net farm income, and in 2000, about 70 percent. Emergency assistance originating from special legislation accounted for $8.9 billion of the direct payments last year. As indicated by the House Agriculture Committee action cited above, supplementals appear to be a foregone conclusion in 2001.

Issues Raised by Supplemental Payments

Who Gets the Money?

With government subsidies accounting for such a large proportion of net income, questions arise as to the equitable distribution among farmers who are recipients. There are some that feel that the extra payments should be targeted to small and mid-sized farmers. Payment limitations, which have never been truly effective, are now even more questionable. The

1996 Farm Bill and its flexibility provisions shifted some program benefits from farmers to landlords. Basing the supplemental payment on the AMTA has shifted support further toward landowners.

Further, it should be noted that the AMTA payments are based on historic payments under the previous commodity programs. Essentially, those who get the payments today are those who were receiving commodity payments in 1995. Thus, those receiving the supplemental payments are not those who are producing the crops today.

What Commodities?

A theory behind multi-year farm bills dealing only with the so-called "major crops" (wheat, feedgrains, cotton, rice, and oilseeds) has been that with so much of U.S. acreage accounted for by these crops, it was unnecessary to deal with scores of minor crops or livestock (except for dairy). These commodities would automatically adjust in price. For example, if a government program boosted the price of feedgrains and oilseeds, their acreage would tend to increase at the expense of minor commodities, causing them to increase in price as well. Soybean growers now demand an AMTA so they can share in the AMTA-based supplementals. Supplementals have been used in hogs, dairy, sugar — even apples. California fruit and vegetable growers have been lobbying Congress for $1.5 billion annually to offset low prices for specialty crops.

Impact on Supply

Relatively strong global grain production has resulted in market prices that signal a contraction in supply. Supplemental payments, along with higher marketing loan payments, give farmers the opposite signal. There is disagreement among economists about the extent to which supplies are increased as a result of these payments. The U.S. will likely argue in the WTO that supplementals distributed as additional AMTA payments are "green box" e.g., they do not distort the market. However, there is little doubt that they keep excess resources in the agricultural sector and, therefore, increase output. With farmers dependent on the payments to repay loans and stay in business, it has become a situation for Congress of "damned if you do and damned if you don't."

Impact on Land Values

Agricultural land prices in major growing areas continue to rise as the value of government payments is capitalized into land values. This, too, is a perverse signal that is just the opposite of what normal economic forces would dictate.

Payment Uncertainty

Another rationale for the passage of multi-year farm legislation is that agriculture, a highly capital intensive industry with few alternative uses for facilities and equipment, benefits from farmers having the knowledge of what the government programs will be over the next several years. *Ad hoc* annual payments do not provide this prior insight. Will the payment be offered again next year? If so, how big will it be? The availability of funds for supplemental payments has, of course, been created by the shift from a budget deficit to a large surplus, but will the surplus last?

Alternatives and Consequences

Status Quo

Although nobody – Congress, the previous or current administration, farmers, taxpayers, or economists – seems to really like the current policy of annual supplemental payments, there has been little momentum for doing something different. Barring a major crop failure somewhere in the world, high taxpayer costs, misleading economic signals, low market prices, and stagnant net farm income is likely with the status quo in 2001 and 2002. The House is attempting to rewrite at least the income support provisions of the farm bill in 2001 (a non-election year). However, there has not appeared to be much support for a 2001 rewrite in the Senate, although the impact of the change to Democratic leadership has yet to be tested. Of course, the specter of reversion to permanent legislation in 2002 means Congress must act by December 31, 2002, unless it extends the 1996 Act.

Countercyclical Payments

The outcry for "countercyclical payments" is almost universal, and is as ironic as well. The entire basis for farm programs for over 60 years was for the government to make direct payments or restrict supply to influence farm prices to rise when they were low, and, likewise, to allow acreage to increase or release stocks to the market when prices were high. This focus of farm policy was largely ignored in the 1996 Farm Act.

So, a return to countercyclicality is a strong likelihood with upcoming farm legislation. Indeed, the "one-shot" annual payments are themselves Countercyclical — as are marketing loan benefits and subsidized crop insurance. Congress has obviously been convinced that agricultural prices and incomes would have been at extraordinary low levels compared to historic norms to enact the supplemental payment levels that it did.

The Commission on 21st Century Production Agriculture recommends the use of supplement countercyclical SIS payments, triggered by gross revenues from program crops falling below some specified historic norm. Most special interest testimony recently before the House Agricultural Committee called for a form of counter-cyclical program provisions although there was no consensus on how to implement it.

A Quid Pro Quo

Most government programs require subsidy recipients to do something in return for payments. With the supplemental payments, one must simply be already receiving AMTA payments and monitoring his or her land in a conserving state, or be in another category singled out for assistance, such as a dairy farmer.

Therefore, one way to change supplementals would be to focus them more into green payments, or some kind of production or inventory adjustment incentive.

As pointed out in a recent *Choices* article by Zulauf et al:

"Provision of supplemental assistance suggests that society is not ready to cut support to the U.S. farm sector, at least not in times of budget surpluses and low farm prices. Farmers depend on farm programs to maintain both their income and their wealth. This dependency makes it easier for non-farm policy actors to negotiate with the farm sector for changes in other parts of the Farm Bill. A similar dependency during the financial crisis of the 1980s helped produce a 1985 Farm Bill with notable environmental provisions including conservation compliance, the Conservation Reserve Program, Sodbuster, and Swampbuster."

No Supplementals

Finally, Congress could simply bite the bullet and not pass supplemental payments in 2001 and beyond. Farmers who have been receiving the payments and their lenders would be drastically affected. Regions in which the supplementals account for the largest proportion of net farm income would bear the brunt of the adjustment process. Many economists believe that in two to three years with no supplemental payments, production of major crops would shrink and prices would rebound to profitable levels. However, others believe that the adjustment would take much longer and that not only farmers but the agribusiness infrastructure — as well as the communities dependent on production agriculture — would undergo substantial financial damage.

Conclusions

Secretary of Agriculture Ann Veneman recently made some intriguing, and for a Cabinet member, extremely provocative remarks about the annual *ad* *hoc* assistance provided by the Congress since 1998: “They do not provide farmers and ranchers or their lenders needed assurance about the role of the federal government in the future.” Further, Veneman stated that such assistance “can also turn into a political bidding war which attempts to relieve the patient’s symptoms without addressing the disease.”

Should the objectives of farm policy be welfare to farm families? If so, the track record has not been so good as pointed out in a number of recent USDA and *Choices* articles. However, if one cuts through the rhetoric and focuses on the evidence, it is clear that at least since the Morrill Act of 1862, the U.S. government and its people have suggested a food security and stability objective. If this is the measure by which governmental programs — including supplemental payments — are to be evaluated, then it would be hard to criticize the results.

References and Suggested Readings

The Commission on 21st Century Production Agriculture. “Directions for Future Farm Policy: The Role of Government in Support of Production Agriculture.” Report to the President and Congress. January 2001.

Zulauf, C., L. Tweeten, and A. Lines. “Pre-FAIR, Post-FAIR...Fair Enough?” Choices (1) 2201 pg. 10.