



2012 Farm Bill Debate: Multiple-Year Risk Assistance Programs

Carl Zulauf, Professor, Ohio State University

September 2012

Most farm safety net provisions in the Farm Bills passed by the full Senate and the House of Representative's Committee on Agriculture can be classified into 3 categories: (1) enhancements to crop insurance, (2) assistance against shallow losses, and (3) assistance against losses that extend across multiple crop years. This farmdoc post focuses on the alternative proposals for multiple-year risk assistance.

Enhancements to crop insurance are largely the same in the Senate and House Committee Farm Bills (see farmdoc post, "First Draft of New House Farm Bill," page 6, July 10, 2012, available here). Moreover, the alternative shallow loss proposals are largely in agreement on their basic design structure, but differ on specific coverage parameters, whether the program should be at the farm or county level, and whether the program should be administered by the Farm Service Agency (FSA) or Risk Management Agency (RMA) (see farmdoc post, "Shallow Loss Programs and the 2012 Farm Bill Debate," August 16, 2012, available here). In the author's opinion, the differences yet to be resolved regarding multiple-year assistance are greater than the differences yet to be resolved in the other two farm safety net policy categories.

Comparison of Multiple-Year Risk Proposals

Taking a broad perspective, three types of multiple-year programs are in the Senate Farm Bill and the House Committee Farm Bill.

One, which is contained in both farm bills, covers a limited, specified range of losses measured at the county level based on a target that is calculated using an Olympic moving average of prices and yield for the last 5 crop years. Thus, its target revenue changes with market conditions, although the target changes slower than the market due to the use of a moving average. This program covers losses that fall between 79% and 89% of target revenue in the Senate Bill and between 75% and 85% of target revenue in the House Committee Bill. Payment is based on a share of current planted acres and acres prevented from being planted. This program also functions as a shallow loss program.

The second multiple-year program, which is only in the Senate Farm Bill, is similar in design to the county revenue program discussed in the previous paragraph, but is sited at the level of the individual farm operation.

The third multiple-year program, which is only in the House Committee Farm Bill, is a variation of the current target price program. The target prices are fixed by Congress for the life of the Farm Bill and, thus, do not adjust upward or downward with changes in the market. Payment is based on historical yield, which can be updated to the 2008-2012 crop years, and on a share of

current planted acres and acres prevented from being planted. In most situations, this program will not function as a shallow loss program.

Policy Issues Framing the Debate over the Multiple-Year Program

The discussion in the preceding section and examination of the farm bill debate suggest that the debate over the design of a multiple-year risk assistance program is being framed by 6 issues:

- (1) Should the target be stated in terms of price or revenue?
- (2) Should the program be at the individual farm or larger area, notably the county?
- (3) Should the multiple-year program be separate or combined with the shallow loss program?
- (4) How much overlap should occur with crop insurance?
- (5) Should the program be administered by FSA or RMA?
- (6) Should the target be fixed or move with the market?

Each of these issues warrant extended discussion, but, due to space constraints and in keeping with the focus of this farmdoc post on the broader issue, the following discussion notes only selected points. Because a comparison of revenue and price programs was provided in the farmdoc post, "Price vs. Revenue Farm Safety Net," August 9, 2012, available here; this issue is not discussed in this post.

Selected Observations on Design Issues

In general, any difference in the value and calculation of parameters between risk programs can create the potential for overlap between the programs or can create gaps in coverage. Overlap means that a farm can receive payments from both programs for the same loss. The overlap between the ACRE program and crop insurance has received a lot of discussion, as has the overlap between the proposed county and farm multiple-year revenue programs and crop insurance. However, overlap can also exist between crop insurance and the fixed target price program. The overlap occurs when a large enough price decline triggers payments by both the target price program and crop insurance. In a budget constrained environment, such as the 2012 Farm Bill, eliminating overlap between programs attracts attention because of the potential for budget savings. Hence, interest exists in creating a combined multiple-year and shallow loss program.

Historically, FSA has administered the farm income programs while RMA has administered the insurance programs. With the emergence of a farm safety net based on risk management, the question has arisen whether both agencies are needed. Again, the underlying reason is the potential to save money in a budget constrained environment. The decision to eliminate an agency means the loss of jobs, which also is a key issue in the current American political dialogue, especially in a Presidential election year. If the decision is made to keep both agencies and assuming a risk management orientation for the farm safety net, one potential alternative for dividing responsibilities among the two agencies is to make RMA responsible for individual insurance products and FSA responsible for the products at larger geographic areas,

such as the county products. A rationale for such a potential division is that farms can make decisions that can influence payments from individual level insurance but are unlikely to influence payments from county level programs in most situations. The ability to influence payments is a management issue for all types of individual level insurance, not just farm insurance. Local insurance agents and independent loss adjusters provide a means for managing these situations. In contrast, county products can be administered at the county or an even larger geographical unit, since payment depends on yield and price for larger geographical units and the acres planted to a crop on an individual farm, which FSA (and RMA) already collects.

All government programs, farm and nonfarm, distort private economic markets. While some distortions are valued by society, most distortions have negative impacts upon at least some economic participants. In terms of farm safety net programs, distortions that are commonly discussed are (1) overproduction, which in turn leads to the over use of inputs as well as to lower prices for agricultural commodities, thus distorting international trade; and (2) higher capital values, notably higher land values. Everything else equal, fixed targets will produce more distortions than market-oriented targets. The reason is that fixed targets provide a floor that will last longer than will a market-oriented target. A market oriented target will eventually move lower, thus providing farms with only a temporary window to make adjustments. The counterpoint is that a market-oriented target generally will provide less multiple-year assistance when a major risk factor happens, such as a prolonged, steep decline in price.

Summary Observations

Both the Senate Farm Bill and House Agriculture Committee Farm Bill contain a program that addresses losses that occur across several years. The former is based on market-oriented revenue targets administered by FSA while the latter is based on targets fixed for the length of the farm bill and administered by FSA. However, these are not the only two alternatives. As discussions occur over how to address the 6 issues that underlie the debate over multiple-year risk assistance, other alternatives could emerge. For example, the final compromise could be a market-oriented price target or a fixed revenue target, neither of which are in the current Farm Bill proposals. Another example is to have RMA deliver multiple-year risk protection by adding to the shallow loss program known as the Supplemental Coverage Option (SCO) that price or revenue associated with SCO can be no lower than either a fixed price or revenue, or a market flexible target price or target revenue. It is worth noting that the fixed price version of this alternative is contained in the House Farm Bill for the cotton STAX (Stacked Income Protection Plan) proposal. In summary, the design of the multiple-year program will rest upon how Congress and farm policy actors answer each of the six underlying issues, both individually and as a group. In the author's view, the design of the multiple-year program is one of the most interesting debates left in the crafting of the next farm bill because of the wide-range of possible outcomes.

This publication is also available at <http://www.farmdoc.illinois.edu/>.