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Capping the Costs of the Two Major New Commodity Programs

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The 2014 farm bill eliminated the infamous direct payments program that gave farmers subsidies regardless of need. Instead of stopping there and making real progress, Congress created two new commodity programs, Agricultural Risk Coverage (ARC) and Price Loss Coverage (PLC), which will likely cost as much as and probably far more than the direct payments program. The farm bill did not limit the liability that taxpayers will incur from these programs. In essence, Congress wrote a blank check.

The House overwhelmingly passed an amendment[1] to its original farm bill (a bill that was voted down) that would have capped the costs of these programs. The same provision was included in the farm bill[2] that was sent to the Senate for conference. Regrettably, the provision was removed during conference.

Both ARC and PLC should be eliminated. In the interim, Congress can adopt the House's commonsense step and provide some reasonable limits to the taxpayers' exposure.

What Are ARC and PLC?

On a crop-by-crop basis, farmers can participate either in the ARC program or in the PLC program. ARC protects farmers from shallow losses (i.e., minor losses), providing payments when their actual revenues fall below 86 percent of the expected revenues for their crops.[3] PLC provides payments to farmers when commodity prices fall below a fixed reference price established by statute.

These two new programs go far beyond providing farmers with a safety net. The ARC program removes virtually all risk associated with producing and marketing the crops that the program covers. Farmers selecting this option receive taxpayer-funded subsidies for even minor losses—losses that often can simply be attributed to normal business risk.[4]

The reference prices in the PLC program were set so high for some commodities that payments will likely be triggered from the outset. For example, the reference price of corn was set at $3.70 per bushel.[5] The annual long-term projections from the U.S. Department of Agriculture (USDA),[6] released 10 days after Congress passed the farm bill, projected corn prices to be lower for all five years (2014–2018) of the farm bill. The average annual price was $3.47 per bushel. Congress chose not to wait for this more accurate data, but instead relied on outdated Congressional Budget Office (CBO) price projections[7] that estimated a $4.53 per bushel annual average price for 2014–2018.

The Costs Already Appear to be Shattering Projections

During the farm bill debate, ARC and PLC critics argued[8] that assuming prices would stay at or near record highs would be problematic because prices would likely fall. As a result, the programs would incur far greater costs than projected.

The critics were proven right. Corn and wheat prices dropped significantly before the farm bill even passed. Nevertheless, Congress used[9] the CBO's

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outdated commodity price projections[10] for ARC and PLC instead of waiting for the USDA's annual long-term projections.

Between using assumptions that did not reflect declining prices and setting reference prices in the PLC program far too high, Congress almost ensured that the ARC and PLC programs would cost far more than projected.

Some experts estimate that ARC and PLC could cost $8 billion (if not more) in the first year alone.[11] The CBO's new January 2015 cost projection for the first year[12] of these programs is $4.4 billion, and its new projected average annual cost for ARC and PLC for the five-year farm bill is $5.3 billion.[13] These projections compare to direct payments that were projected to cost about $4.5 billion[14] annually if they had not been eliminated.

Based on the CBO's cost projections immediately before the farm bill passed, these programs would have cost $3.8 billion in the first year and averaged about $3.6 billion annually. Both figures are significantly lower than the projected costs just released by the CBO.[15]

1. H.Amdt. 179 to H.R. 1947, 113rd Cong., 1st Sess., June 19, 2013, https://www.congress.gov/amendment/113th-congress/house-amendment/179?q=%7B%22search%22%3A%5B%22h.r.+1947%22%5D%7D (accessed February 6, 2015). The amendment passed by a 267–156 vote. For the roll call vote, see U.S. House of Representatives, Office of the Clerk, "Final Vote Results for Roll Call 257," June 19, 2013, http://clerk.house.gov/evs/2013/roll257.xml (accessed February 6, 2015).
2. H.R. 2642, 1107(e), engrossed in House, July 11, 2013, https://www.congress.gov/bill/113th-congress/house-bill/2642/text/107855 (accessed February 6, 2015).
3. Subsidies are paid when actual revenue falls below 86 percent of historical or benchmark revenue. To learn more about how benchmark revenue is determined, see U.S. Department of Agriculture, "Crop Commodity Programs," http://www.ers.usda.gov/agricultural-act-of-2014-highlights-and-implications/crop-commodity-programs.aspx (accessed February 6, 2015), and Agricultural Act of 2014, Public Law 113–79, § 1117 (c), http://agriculture.house.gov/sites/republicans.agriculture.house.gov/files/pdf/legislation/Final_AgAct2014.pdf (accessed February 6, 2015).
4. For a discussion of the problems with a shallow loss program, see American Farm Bureau Federation, letter to the Committee on Agriculture, Nutrition and Forestry, U.S. Senate, and the Committee on Agriculture, U.S. House of Representatives, October 17, 2011, http://farmpolicy.com/wp-content/uploads/2011/10/101711_FarmBureau_FarmBillShallowLoss.pdf (accessed February 6, 2015). The letter was written when the discussion regarding shallow loss revenue coverage was at 90 percent. While the numbers have been reduced slightly, the same general concerns about shallow loss highlighted in this paper would still apply.
5. Public Law 113–79, §1111 (18)(B).
6. Paul Westcott and Ronald Trostle, "USDA Agricultural Projections to 2023," U.S. Department of Agriculture, Economic Research Service, February 2014, pp. 54–75, http://www.ers.usda.gov/publications/oce-usda-agricultural-projections/oce141.aspx (accessed February 4, 2015).
7. Congressional Budget Office, "CBO's May 2013 Baseline for Farm Programs," May 14, 2013, https://www.cbo.gov/sites/default/files/cbofiles/attachments/44202-2013-05-USDA.pdf (accessed February 4, 2015).
8. For example, see Daren Bakst, "Proposed New Farm Programs: Costly and Risky for Taxpayers," Heritage Foundation *Backgrounder* No. 2815, June 14, 2013, http://www.heritage.org/research/reports/2013/06/proposed-new-farm-programs-costly-and-risky-for-taxpayers (accessed February 6, 2015), and Vincent H. Smith and Barry K. Goodwin, "The Devil Is in the Details: Base Updating and the Cost of New Farm Bill Programs," American Enterprise Institute, January 7, 2013, http://www.aei.org/wp-content/uploads/2014/01/-the-devil-is-in-the-details-base-updating-and-the-cost-of-new-farm-bill-programs_120213508400.pdf (accessed February 6, 2015).
9. Douglas W. Elmendorf, letter to Representative Frank D. Lucas (R–OK), January 28, 2014, http://www.cbo.gov/sites/default/files/cbofiles/attachments/hr2642LucasLtr.pdf (accessed February 4, 2015).
10. Congressional Budget Office, "CBO's May 2013 Baseline for Farm Programs."
11. Ros Krasny and Christine Stebbins, "US Farmers Set to Get Huge Government Payouts Despite Bumper Harvest," Reuters, November 19, 2014, http://www.reuters.com/article/2014/11/19/usa-grains-insurance-idUSL2N0T122P20141119 (accessed February 4, 2015).
12. Total expected costs of the programs for the five-year farm bill should not be based on one year alone, but the likely first-year burden on taxpayers already demonstrates the scope of the taxpayers' financial exposure—a level of exposure that could grow even worse.
13. Congressional Budget Office, "CBO's January 2015 Baseline for Farm Programs," January 26, 2015, http://www.cbo.gov/publication/44202 (accessed February 4, 2015).
14. Congressional Budget Office, "CBO's May 2013 Baseline for Farm Programs." The 2014 farm bill also ended countercyclical payments and the Average Crop Revenue Election (ACRE) program. Average annual cost projection for direct payments, countercyclical payments, and ACRE combined for 2014–2018 was $5.4 billion. The cost of the ARC and PLC programs will likely equal or cost more than all of these programs combined.
15. Elmendorf, letter to Representative Frank D. Lucas.

What Should Congress Do to Protect Taxpayers?

Congress should eliminate the ARC and PLC programs. They are unnecessary and costly, and they provide subsidies that effectively eliminate most risk. In addition, the programs impose open-ended financial exposure to taxpayers. Until the programs are eliminated, Congress should address this unacceptable exposure for taxpayers. It does not even need to touch the substance of those programs to provide some protection for taxpayers.

Finishing What the House Started. The House farm bill would have limited taxpayer exposure to 110 percent of CBO cost projections for these programs. The language specified a cap of about $17 billion.[16] If using 110 percent of the CBO cost projections for ARC and PLC prior to passage of the farm bill, these programs would cost $19.7 billion for the five-year farm bill.[17]

Congress should adopt a cap, using the $19.7 billion limit for total costs. To implement this, the best approach would likely be to set a cap for each year. The amount could not exceed the average per year of about $3.94 billon. In a year in which costs were below this number, the USDA could roll over the money for future years.[18] If costs exceeded the annual cap, program participants would simply receive a prorated share of their subsidies.

At Most, the Costs Should Not Exceed the Costs of Direct Payments. The possibility that ARC and PLC could cost far more than direct payments is something Congress should want to prevent (and be embarrassed about). Taxpayers should not pay more than what they would have paid under direct payments (about $4.5 billion a year). If the cap is based on direct payments, it would be $22.5 billion for the five-year farm bill.[19]

A Commonsense Reform

The ARC and PLC programs should be repealed, but Congress can at least protect taxpayers in the interim by capping the costs of ARC and PLC.[20] ARC and PLC would still remain in place, but taxpayers would have some certainty that these overly generous programs would have some limit on the burden they place on taxpayers. However, a cap would not end the need for Congress to eliminate ARC and PLC—it would simply help to “reduce the bleeding.”

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16. The language specified a cap of about $17 billion for fiscal year (FY) 2014–FY 2020, which covers the 2014–2018 crop years. There is a two-year time lag between the crop year and when payments are made (e.g., payments for the 2014 crop year will not start until FY 2016, and payments for the 2018 crop year will not start until FY 2020).
17. Elmendorf, letter to Representative Frank D. Lucas. The costs are based on FY 2016–FY 2020.
18. If payments do not reach the cap at the end of the farm bill, this would be savings for taxpayers.
19. While the cost of direct payments should be the highest level of any cap, even a cap covering direct payments, countercyclical payments, and ACRE would be about $27 billion based on projected costs for 2014–2018 and possibly less than what the total costs for ARC and PLC will be.
20. For those who think a cap is unnecessary because the projected costs will not be exceeded (which is unlikely), such a measure should be a non-issue.