



Tom

UNITED STATES DEPARTMENT OF AGRICULTURE

OFFICE OF THE SECRETARY

TELEPHONE (202) 720-3631

FAX (202) 720-5437

FAX COVER SHEET

DATE: 11/2

NUMBER OF PAGES 4, INCLUDING COVER SHEET

PLEASE DELIVER TO:

Mary Smith

FAX NUMBER: ()

456-7431

PHONE ()

FROM: ☐ DAN GLICKMAN, SECRETARY

☐ JOHN GIBSON, SPECIAL ASSISTANT

☐ GREG FRAZIER, CHIEF OF STAFF

☐ KOFI DEGRAFT-JOHNSON, EXECUTIVE ASSISTANT

☒ PATRICK STEEL, DEPUTY CHIEF OF STAFF

☐ SEAN O'SHEA, EXECUTIVE ASSISTANT

☐ PAUL DRAZEK, SPECIAL ASSISTANT FOR FOREIGN POLICY

☐ ERIC OLSEN, COUNSEL TO THE SECRETARY FOR DOMESTIC POLICY

☐ JANET POTTS, COUNSEL TO THE SECRETARY

☐ JOHN SPARKS, SPECIAL ASSISTANT FOR CIVIL RIGHTS

☐ LAURETTA MILES, ADMINISTRATIVE ASSISTANT

MESSAGE:

Sorry This took a while.
Call w/ questions.



DEPARTMENT OF AGRICULTURE
OFFICE OF THE SECRETARY
WASHINGTON, D.C. 20250
October 21, 1998

Honorable Jacob J. Lew
Director
Office of Management and Budget
Room 252, Old Executive Office Building
Washington, D.C. 20503

Dear Jack:

On September 28, 1998, I wrote to submit the Department of Agriculture's (USDA) budget proposal for fiscal year (FY) 2000. At that time, I promised further detail regarding the policy recommendations we propose for strengthening the "farm safety net."

These recommendations, contained herein, are made to satisfy President Clinton's request, and our joint promises, to assist America's farm families who are facing declining prices and devastating production losses. The President has repeatedly stated his doubts about the effectiveness of the current "safety net" available to our farmers, along with his commitment to fix the problems that have come to light.

During the past 5 years, we have seen dramatic changes in the network of Federal programs designed to give farmers a meaningful "safety net" against adversity, most dramatically in the 1994 Federal Crop Insurance Reform Act and in the 1996 Farm Bill. This year, the 1994 and 1996 changes to the program are being tested for the first time under highly difficult circumstances that include multi-year disasters, El Niño and La Niña, a historic drought, serious declines in prices for major commodities, and, finally, disease and insect outbreaks in many parts of the country.

As with any new program being tested under fire for the first time, many flaws have become clearly apparent, along with many positives. The reformed crop insurance program has worked well in most respects. Today, about 80 percent of the nation's crop production is insurable and about 63 percent of acres with insurable crops participate in the program. This compares with a level of under 40% participation in 1994. Farmer choices and program features have also been greatly improved over the years.

On the negative side, however, we have also seen significant impact. When multiple-year losses occur, insured yields tend to diminish and farmer premiums rise in relation to the benefits received. In addition, there are gaps in coverage. The premium-free catastrophic (CAT) level of insurance does not provide adequate level of protection for most producers, and higher levels of "buy-up" coverage are more costly than many producers are willing or able to pay. As a result, too many farmers are either uninsured or under-insured.

The fact that the Administration found it necessary to propose an emergency supplemental relief package to address the current farm crisis testifies to the continuing need to revisit the adequacy of the existing safety net fabric.

Because disaster response is one of the most important responsibilities that any government owes to its citizens, I regard the improvements of the farm safety net as perhaps the most pressing and most challenging items on my agenda as Secretary of Agriculture. We must make our Federal crop insurance program fairer, more affordable, and more functional. The proposals I am sending forward today will create a strong safety net to support more fully our American farm producers. The proposals contain clear improvements in policy items while rectifying years of under-funding for USDA's base programs. They raise the basic safety-net floor, while providing farmers with greater incentives to obtain higher coverage levels. Resources are made available to help agricultural producers purchase better protection against recurring crop losses and falling prices. A common trigger for emergency-based programs is created for the Secretary to make help available more quickly. Finally, farmers are provided with access to the newest information available in order to equip them to become more active and effective risk managers.

We expect that these changes will cause many more farmers to participate in crop insurance at higher levels. We believe participation levels may rise to as high as 80 percent. Among other things, the amount of subsidy provided by the Federal government for farmer premiums, which is currently 38 percent of buy-up coverage, will rise to approximately 51 percent. RMA will continue to fully subsidize CAT coverage and increase coverage levels from 50/55 percent to 60/70 percent. Furthermore, RMA also plans to increase additional coverage levels from 65 to 70 percent. As a result of these changes, producers will pay less for greater amounts of coverage and could receive approximately \$1.7 billion more in indemnity payments during crop year 2000. Farmer choices are expanded by challenging private industry to create new products in response to new economic incentives as well as by providing greater flexibility to RMA in developing new pilot approaches.

As President Clinton has pointed out, while "... there are some people who think this system is fine the way it is ... I don't. I think the current system will reduce the number of family farmers, even if it doesn't reduce the acreage being farmed. And I don't think that's a good thing for America. So I would like to see a system where farmers don't fail because of acts of God ... At this moment of prosperity for our nation, we are certainly able to, and we clearly must, help our neighbors on the farm throughout this current crisis so that we can strengthen our rural communities for the 21st century."

I hope you will give our proposal your fullest attention and consideration. We believe that we are presenting you with a balanced approach that will address the President's concerns with improving the financial base for farm producers and rural communities across America.

Sincerely,

A handwritten signature in black ink, appearing to read "Dan", with a long horizontal stroke extending to the right.

DAN GLICKMAN
Secretary

Proposal Choices

Costs At-A-Glance

Section I: Improving Insurance Options subtotal up to \$2,346 million

Making Insurance Affordable for Farmers

1. Increase Subsidy Levels for Crop Insurance (up to \$1,280 million)
2. Bolster Catastrophe (C.A.D.) Coverage (\$500 million)
3. Create Multi-year Disaster Coverage (up to \$310 million)
4. Offer Deductible Recovery Coverage (Disappearing Deductible) (up to \$500 million)

Speeding Risk Management Tools to Market

5. Increase Flexibility for Pilot Projects (no budget impact)
6. Accelerate New Product Development (up to \$10 million)
7. Streamline the Regulatory Process (no budget impact)

Section II: Accelerating USDA Emergency

Responses

subtotal up to \$628 million

8. Expedite Emergency Response Procedures (up to \$24 million)
9. Allow Multiple Emergency Benefits (up to \$10 million)
10. Overhaul the Noninsured Assistance Program (NAP) (up to \$479 million)
11. Expand the Emergency Conservation Program (ECP) (up to \$15 million)
12. Bridge Emergency Loans Gap - Farm Service Agency (FSA) and Small Business Administration (SBA) (up to \$600 million)

Section III: Communicating Change

subtotal up to \$89.7 million

13. Create Pilot Programs for Communities and Livestock (KOP) (\$29.5 million)
14. Train More Farmers to Be Active Risk Managers (\$29.2 million)
15. Improve Service for Small Policyholders (\$40 million)

GRAND TOTAL \$3,967.7 million



DEPARTMENT OF AGRICULTURE
OFFICE OF THE SECRETARY
WASHINGTON, D.C. 20250

October 15, 1998

*Franky
Farms*

MEMORANDUM FOR BRUCE REED

FROM: Patrick Steel
Deputy Chief of Staff

SUBJECT: Farm Numbers

The following statistics reflect the decline in all farms throughout America for the years including 1950, 1980, 1992, 1995, and 1997:

<u>YEAR</u>	<u>NUMBER OF FARMS</u>	<u>DECLINE FROM PREVIOUS</u>
1950	5,648,000	N/A
1980	2,444,000	3,204,000
1992	2,094,000	350,000
1995	2,068,000	26,000
1997	2,058,000	10,000

According to the 20th Annual Family Farm Report to Congress of 1995, 98% of all farms are defined as "family farms", with the remaining 2% considered non-family farms. Family farms are considered those farms organized as sole proprietorships, partnerships, or family corporations controlled by one or more households. According to the 1998 National Commission on Small Farms Report, small farms (defined as those farms with less than \$250,000 gross receipts annually on which day-to-day labor and management are provided by the farmer and/or the farm family that owns the production or owns, or leases, the productive assets) account for 94% of all farms within the U.S.

I hope this is helpful.

Attachment



On farm for you

UNITED STATES DEPARTMENT OF AGRICULTURE

OFFICE OF THE SECRETARY

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MESSAGE: _____

Private Sector Proposal - On Farm research
part

BEEF INDUSTRY FOOD SAFETY COUNCIL

Summary of Needed Research and Projected Funding Level

could be
split b/w
internal (ARS) +
external
(CSREES)

I. PREHARVEST RESEARCH (\$20 million total)

- Gain a better understanding of the host/pathogen relationship to aid in the identification of potential pre-harvest critical control points and intervention strategies (\$2 million/year for 5 years / \$10 million).
- Identify production and management practices that influence growth, shedding and spread of *E. coli* O157:H7 (\$1 million/year for 5 years / \$5 million).
- Gain a better understanding of the ecology of *E. coli* O157:H7. (\$1 million/year for 5 years / \$5 million)

II. BEEF CARCASS CONVERSION (\$9.0 million total)

- Develop a system of microbiological verification of the slaughter process for beef. (2 years / \$4.3 million total).
- Demonstration project of the microbial advantages of utilizing multiple new technologies in the slaughter process. This study will be utilized to facilitate regulatory changes (2 years / \$3.1 million -assuming 1 pilot plant; each additional plant = \$3.0 million).
- Develop benchmarking data on microbial profiles/potential recontamination of product during the carcass conversion process (2 years / \$1.6 million)

III. GROUND BEEF PROCESSING (\$9.35 million total)

- Develop sampling and testing protocol and recommend microbiological testing as an integral verification step of all processing leading to the manufacture of ground beef (5 years / \$1.5 million).
- Develop protocol for testing for *E. coli* O157:H7 that facilitates the definition of lot size (2 years / \$0.6 million).
- Develop irradiation guidelines for ground beef products (3.5 years / \$5.65 million).
- Microbiological enumeration of pathogenic microbial loads in ground beef (1 year / \$0.1 million).
- Research new microbial intervention systems for ground beef and cooking systems for beef patties (3 years / \$1.5 million).

IV. RETAIL/FOODSERVICE (\$1.0 million total)

- Determine the microbiological profiles for beef raw materials and finished ground beef product from production to retail (1.5 years / \$0.3 million).
- Assessment of the microbial effect of needle tenderizing and lack of cooking and preparation standards for such products (1 year / \$0.5 million).
- Development of a common strategy and tools of management that provide a uniform system of assessment and administration of food safety management at retail and food service establishments (1.5 years / \$0.2 million).

BEEF INDUSTRY FOOD SAFETY COUNCIL

RESEARCH/SCIENCE WORKING GROUP RECOMMENDATIONS

PRE-HARVEST SEGMENT

The presence of *E. coli* O157:H7 in the general cattle population suggests that preventative strategies prior to harvest may potentially reduce the incidence of *E. coli* O157:H7. Efforts to establish points critical for incidence reduction are needed to address the efficacy of pre-harvest interventions and strategies.

Initially, however, more fundamental studies are required as a necessary prerequisite for directing efforts towards pre-harvest strategies to reduce the incidence of *E. coli* O157:H7. The priorities for pre-harvest research are:

- (1) **Gain a better understanding of the host/pathogen relationship to aid in the identification of potential pre-harvest critical control points and intervention strategies.**
 - * Establish defined protocols and procedures for measuring the prevalence of *E. coli* O157:H7. Timeline – 1 year
 - * Where data are lacking or inconclusive, establish the prevalence of *E. coli* O157:H7 in segments of the beef production sector – farm, ranch, backgrounding, feedlot – and the relation between variables such as animal age, type and productive status and *E. coli* O157:H7 prevalence. Timeline – 2 years
 - * Determine reservoirs for *E. coli* O157:H7 such as birds, rodents, other wildlife, bird droppings and other domestic animals and establish the distribution and survival in the environment, e.g., manure, soil, water, lagoons and feeds. Timeline – 4 years
 - * Improve knowledge of the epidemiology of O157:H7 in cattle – how it spreads, colonizes cattle, levels of exposure and time required for colonization and clearing of the organism, individual animal versus herd incidence, geographical distribution. Timeline – 5 years

Budget required – \$10 million

(2) Identify production and management practices that influence growth, shedding and spread of *E. coli* O157:H7

- * Determine the level of contamination on hides and hair of cattle at slaughter plants and factors that affect level of contamination. Timeline – 1 year
- * Investigate management variables such as diet ingredients, feed and water additives, growth promotants,, time-on-feed, health management practices and health status, stress and handling, production facilities management practices, and feed withdrawal. Timeline – 2 to 3 years
- * Understand the effect of modern production practices on the diversity and properties of *E. coli* O157:H7 populations and the emergence of new foodborne pathogens. Timeline – 5 years

Budget required – \$5 million

(3) Gain a better understanding of the biology and ecology of *E. coli* O157:H7

- * Determine the affects of rumen variables such as pH, volatile fatty acids and other metabolites. Timeline – 2 years
- * Establish and understand the mechanisms of colonization of the rumen and intestinal tract of cattle. Timeline – 4 years
- * Understand the interactions with either rumen microflora. Timeline – 4 years
- * Determine how *E. coli* O157:H7 acquires acid tolerance and the mechanisms that confer acid tolerance. Timeline – 4 years
- * Conduct a detailed genetic characterization of *E. coli* O157:H7 as contrasted with generic and non-pathogenic *E. coli*. Timeline – 5 years
- * Implement applied/intervention research based on knowledge of the basic biological properties obtained from the preceding research efforts.

Budget required -- \$5 million

2/18/98

Agenda for Rural America

A. What we've done

- Farms
- Transportation
- Education
- Medicine

B. What we can do

- Insurance
- Accounts

C. Timetable

- Meetings
- Memo

2/18/98

Agenda for Rural America

A. What we've done

- Farms
- Transportation
- Education
- Medicine

B. What we can do

- Insurance
- Accounts

C. Timetable

- Meetings
- Memo

high policy
issue
2/18/98

NEC - high
UP. high →
DPL -
DBM -
Sushu

Agenda for Rural America

A. What we've done

- Farms → high
- Transportation
- Education ✓
- Medicine (high)

B. What we can do

- Insurance → high insurance
- Accounts - IRA

C. Timetable

- Meetings
- Memo

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→ Safety net issues

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March 20th / April 7th 1998

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- Meeting -
- Comm. groups
- crop insurance
- social development
- consultation

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DEPARTMENT OF AGRICULTURE
OFFICE OF CONGRESSIONAL RELATIONS
WASHINGTON, D.C. 20250-0100

Farness

FAX COVER SHEET

DATE: 7-7-97

COVER SHEET PLUS 2 PAGES

TO: Tom Freedman

FAX # 456 - 7431

PHONE # _____

FROM: Dave Carter

USDA - OFFICE OF CONGRESSIONAL RELATIONS
ADMINISTRATION BUILDING - ROOM 213A
JEFFERSON DRIVE, S.W.
WASHINGTON, D.C. 20250
(202) 720-7095

REMARKS: _____

102
VA Tobacco Farmers-Goode, 450

Tobacco farmers share settlement concerns with congressman

DANVILLE, Va. (AP) After a scorching day in the fields, a group of Southside Virginia tobacco growers met with their congressman to vent their frustrations with the proposed tobacco industry settlement.

"There's a saying that the road to hell is paved with good intentions," J.T. Davis of Nathalie said Thursday. "If we don't get things turned around, this is going to be the road to hell for the tobacco farmers."

U.S. Rep. Virgil Goode promised to work to get protections for farmers included in the settlement as it makes its way through Congress, particularly measures that would keep the price and supplies of tobacco from plummeting.

"Two factors have got to be market stability and price stability," said Goode, a Democrat from Rocky Mount whose district includes most of Virginia's tobacco farms.

"If you destroy the American tobacco grower, you're still going to have cigarettes; people are still going to smoke," Goode said. "It would just transfer production to countries like China and Brazil."

The farmers said they are worried that the \$360 billion settlement will force cigarette companies to cut their losses by buying cheaper foreign-grown tobacco. They also fear that Congress will reduce or eliminate programs that prop up the price and supply of U.S. tobacco.

"We're not getting rich," said Dick Conner of Halifax County. "It's hard work and it's hot."

The farmers said they're also steamed that they were left out of the proposed settlement, which would allocate millions of dollars to help people quit smoking and compensate sporting events and teams for the loss of tobacco sponsors.

"I don't know of anybody more addicted to tobacco than tobacco growers," Davis said.

But C.D. Bryant of Pittsylvania County said, "We're not looking for some big handout."

This year, tobacco is growing on about 8,400 Virginia farms with projected cash receipts of nearly \$200 million, making it Virginia's most important crop economically.

Gov. George Allen announced Wednesday that he had appointed a three-member task force to work with Congress to minimize the damage the tobacco deal could do to Virginia's \$5 billion-a-year tobacco industry.

President Clinton and Congress must approve the settlement tobacco companies reached with the 40 states that sued them to recover smoking-related health costs.

Under the agreement, all states would be reimbursed for their Medicaid expenses for treating victims of tobacco-related illness.

The attorneys general who negotiated the deal said they wanted to protect tobacco growers and tried to write safeguards for them into the deal, but ultimately left that to Congress.

"If anybody in Washington has a heart or a conscience they are going to put something in this for the growers," Davis said.

(PROFILE

(CAT:Agriculture;)

(CAT:Political;)

(SRC:AP; ST:NC;)

)

AP-NY-07-04-97 0538EDT

SUBJECT: VA AGRI NC POL

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Received by NewsEDGE/LAN: 7/4/97 5:42 AM

KY Tobacco Farmers, Bjt, 0718

(102)

Farm leaders work for relief proposals

LOUISVILLE, Ky. (AP) There are signs that farmers will come out of the legislative process in better shape than they did under last month's \$368.5 billion tobacco settlement.

Kentucky and North Carolina farm leaders are working on a package of relief proposals. Also, a key tobacco industry negotiator appears supportive of the farmers, and health advocates say they want to protect the growers from sudden economic upheaval.

"I feel very strongly that farmers should not be left out of the deal," David Kessler, former commissioner of the U.S. Food and Drug Administration, said recently. "I think that's a very high priority."

These groups don't necessarily agree, however, on the form aid for farmers should take. The options include compensation for lost income, limits on the amount of foreign-grown tobacco in American cigarettes and a buyout program to encourage farmers to stop growing tobacco.

Economic projections show the cutback in smoking that results from the agreement could translate into more than a 50 million-pound reduction in the use of burley leaf, most of which is grown in Kentucky.

With a selling price close to \$2 a pound, that's a lot of lost money.

But the only thing the deal does for farmers is guarantee that the FDA's enhanced regulatory authority won't extend to tobacco cultivation.

The settlement, however, is far from settled. The agreement must be drafted into legislation, passed by Congress and signed by President Clinton.

A lead industry negotiator, North Carolina lawyer J. Phil Carlton, says he wants to help the farmers.

Carlton, the son of a tobacco farmer and until recently the owner of a tobacco farm, told The Courier-Journal last week that the farmer issue will definitely be on the table as negotiators draft the legislation to submit to Congress.

"We're willing to talk about that," Carlton said of one possibility the growers are interested in: a guarantee that cigarette makers will commit to use a certain amount of domestic tobacco.

The industry, according to Carlton, also is willing to consider paying for tobacco crop insurance and the tobacco price-support program's administrative costs should Congress cut off the funding, as some have proposed.

And public health officials want to see the farmers get help, although their main objective is not compensation.

Instead, the health groups want to use money to entice the farmers out of the tobacco business and out of their longstanding political alliance with the cigarette companies.

Their idea is either to pay farmers to retire their growing quotas or give them money to try alternative crops.

Last month, health group negotiators proposed that the settlement set aside about \$150 million a year mainly for that purpose. But Carlton said he rejected that idea, and it was not included in the settlement. He said the proposal was not comprehensive enough.

One of four interagency panels President Clinton set up to review the agreement will focus on the tobacco industry, including the economic impact on the growers.

Unlike the cigarette makers, the farmers come to the legislative process seemingly unblemished by the controversy and distrust that for decades gripped the smoking issue.

"They've not been willing conspirators. They've been pawns," Indiana Attorney General Jeff Modisett said.

Sen. Wendell Ford of Kentucky has said repeatedly that without protection for the farmers, he won't support implementation of the bill.

Ronny Pryor, chief lobbyist for the Kentucky Farm Bureau, wants farmers compensated for lost sales and quota reductions, and he insists there would be little interest among burley growers in a quota buyout. Tobacco is too lucrative to give up, he said.

But Pryor indicated there is nevertheless room to please both farmers and the anti-smoking side. He suggested the possibility of a compromise that would compensate farmers while also helping them move into alternative crops. "We don't see it as an either-or thing," he said.

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Received by NewsEDGE/LAN: 7/4/97 5:45 AM

MEMORANDUM

TO: TOM FREEDMAN
FROM: MARY L. SMITH
RE: ISSUES FOR USDA ECONOMISTS
DATE: JULY 14, 1997

Farmers

- List the tobacco producing states and the number of tobacco farmers per state, and the number of acres per farmer
- Statistics on the number of farmers who farm their acres outright and those who lease their tobacco plot
- Describe the difference between the economics of flue-cured tobacco (primarily in NC?) with the burley tobacco industry (Kentucky?)
- List the percentage of tobacco's total contribution to each state's economy, and statistics in past years
- List the total number of jobs per state that depend on the tobacco industry, include farmers, manufacturers, suppliers, and other tobacco-affected jobs
- List the total dollar amount of the cash crop for tobacco per year
- List what percentage of U.S. tobacco is exported
- describe generally the crop insurance program and how much money is invested each year
- describe the quota system and how the government buys the excess
- describe if there is any law that requires a percentage of U.S. tobacco in U.S. cigarettes
- Describe the extent to which tobacco farmers are already growing alternate crops
- Estimate how much in total dollars it would cost to buy out all the tobacco farmers; also estimate the other effects the buyout would have in other industries and for each state's economy
- identify any issues relating to sustainable agriculture

- *season shifts, trends picture.*



EXECUTIVE OFFICE OF THE PRESIDENT
COUNCIL OF ECONOMIC ADVISERS
WASHINGTON, D.C. 20500

*Farmers
(Not placed)
EW*

SENIOR ECONOMIST

February 9, 1998

TO: THOMAS FREEDMAN, DOMESTIC POLICY COUNCIL
FROM: KEITH FUGLIE *Keith Fuglie*
RE: Agricultural risk management options

In our recent meeting, I agreed to send you a brief memo on pros and cons of some proposed new alternatives for helping farmers manage risk.

Issue

Agriculture tends to be riskier than most businesses, due to two factors. First, production in any given season is highly dependent on environmental factors such as weather and the severity of pests and diseases. Crop production is considerably more variable than livestock production. Second, small changes in aggregate annual production can cause relatively large changes in market prices. Thus, farmers face relatively high levels of annual and seasonal variation in their production and in prices received for their commodities.

By reducing the influence of agricultural programs on commodity prices, the 1996 Farm Act may have increased uncertainties faced by farmers somewhat. However, it also provided farmers with more flexibility in reacting to market conditions, which could serve to reduce market instability over time. For example, U.S. farmers responded to high soybean prices in early 1997 by increasing their soybean plantings. As a result, they produced a record crop, helped build up depleted soybean stocks, and unusually high prices fell back to within a normal range.

Managing risk

Agricultural producers use a variety of means to manage the inherent risks of farming. Traditional risk management tools include storing crops, diversifying production and sources of income (including seeking off-farm employment), and deferring large capital purchases in years of low income. Through access to credit and financial markets, farmers can accumulate liquid assets in good years or retain unused lines of credit to carry them through poor years. In addition, farmers can mitigate risks by using an assortment of new marketing tools, such as forward contracting, options and futures markets, and by purchasing crop insurance.

The USDA offers substantial assistance to farmers for risk management. The USDA subsidizes about 60 percent of the average cost of crop insurance. Although crop insurance is not available for all commodities, its range is steadily being expanded. Most recently, the USDA announced new insurance programs for dryland forage crops and dairy prices. The USDA is also experimenting with crop revenue insurance, which manages yield and price risk for specific crops.

Two additional options that you raised are (1) farmer tax-deferred savings accounts, and (2) whole-farm revenue insurance. Some pros and cons of these options are described below.

Tax-deferred savings accounts

Through a tax-deferred savings account, farmers could make deposits in years of relatively high income and withdrawals in relatively poor years. The principal benefit over other types of savings accounts is that farmers may qualify for a lower marginal tax rate in the year in which a withdrawal is made. Additional features may include a government matching contribution up to some maximum amount, and/or an interest rate bonus on current balances. Canada offers its farmers a Net Income Stabilization Account (NISA) which has both of these features.

Advantages of tax-deferred savings accounts

- they would more directly protect farm income than other insurance programs;
- they would provide benefits to farmers who are currently not eligible for other agricultural insurance programs, such as producers of livestock and speciality crops;
- the subsidies are not likely to distort agricultural markets, as might price supports or guarantees.

Disadvantages

- benefits to farmers from income-smoothing would not be realized for several years, until they had built up balances in the accounts;
- most of the benefits would go to larger farmers. A large proportion of farmers report negative or very low net farm income. For example, in 1993 (a fairly typical farming year), the median net farm income reported for tax purposes was only \$11,300 for farmers who received at least half of their total tax income from farming. Nearly 20 percent of these farmers reported net farm losses. It is unlikely that low-income farmers could benefit from a lower marginal tax rate, since many will already be at the lowest marginal rate or pay no income taxes on farm income at all;
- use of the accounts may simply substitute for other forms of savings;
- farmers may use less of other risk management tools, such crop insurance;
- farmers may choose not to withdraw from accounts in poor years, instead wishing to save balances for retirement. This has been the experience of the Canadian program.

Whole-farm revenue insurance

Unlike current crop yield or crop revenue insurance programs, this option would extend insurance to the entire portfolio of farming operations, including livestock production and crops not included in current insurance programs, such as specialty crops. Farmers would pay an insurance premium (subsidized by the government) at the beginning of each year to insure some minimal level of income, say an average of the previous 5 year's income.

Many of the pros and cons are similar to those of tax-deferred accounts.

Advantages of whole-farm revenue insurance

- it would more directly protect farm income than other insurance programs;
- it would provide benefits to farmers who are currently not eligible for other agricultural insurance programs, such as producers of livestock and speciality crops.

Disadvantages

- most of the benefits would go to larger farmers.
- use of the accounts may simply substitute for other forms of savings;
- farmers may use less of other risk management tools, such as crop insurance;
- farmers may switch to producing more risky commodities or, become locked in to a certain set of farm enterprises.

Points to consider

One of the main objectives of the proposed options is to extend tools for managing risk to producers of livestock and speciality crops, commodities not currently covered by crop insurance programs. As previously mentioned, the USDA is working to extend crop insurance to a broader set of commodities. Further, many specialty crops are subject to marketing orders that regulate market supply, thus reducing market price fluctuations. Regarding livestock, the main source of risk is market price fluctuation, not production (with the exception of the occasional severe disease, such as foot and mouth disease affecting cattle). Producers of most livestock commodities can currently manage price risk by hedging with futures and options contracts. In addition, an increasing share of livestock production is produced under contract with meat processing companies, in which prices are specified in the contracts and less subject to market fluctuations. Finally, note that the risks faced by producers of livestock and speciality crops are no different now than in the past, since these commodities (with the exception of dairy) historically have not had commodity programs and thus were largely unaffected by the 1996 Farm Act.

This assessment is meant to be rather general. I would be happy to provide more detailed assessments of specific options, should the need arise.

cc Jeffrey Frankel, Michele Jolin, Joseph Glauber



Do Farmers Need Tax-Deferred Savings Accounts to Help Manage Income Risk?

Farmers' incomes vary with market conditions and yields. The Federal Agriculture Improvement and Reform Act of 1996 places more risk management responsibility on farmers. Savings accounts are one mechanism that could help farmers manage their income variability. Tax incentives have been proposed to encourage the use of such savings accounts, with benefits expected to accrue both to individual farmers and their communities. Participation rules tied to farm income may favor larger, more prosperous farmers. Because many farmers already save or use other methods to smooth household consumption, tax-advantaged accounts may largely substitute for existing risk management methods and offer limited additional overall benefits to the farm sector and rural areas.

Special accounts, known as tax-deferred savings accounts, that shelter savings and interest income from Federal and State income taxation could help some farmers manage variability in farm income much as Individual Retirement Accounts (IRA's) enhance retirement savings. By depositing income into these accounts during years of high net income, farmers could build a reserve fund for withdrawal during years with abnormally low income. Farmers would be better able to smooth their household consumption over time and self-insure some of their income risk. Taxpayers may benefit if additional financial diversification and liquidity reduce the need for farm disaster relief or continued income support programs.

The Federal Agriculture Improvement and Reform Act of 1996 (hereafter referred to as the 1996 act) reduces the level of price supports and, in some cases, may increase the variability of net farm income by separating Government payments from market prices. Fixed cash transition payments have replaced deficiency payments, which were designed to increase as market prices decreased. Low loan rates for nonrecourse commodity loans will typically not increase farm income during most years. Farmers, therefore, have more responsibility to manage risk despite the availability of transition payments and are being encouraged to learn more about risk management alternatives. Marketing techniques, including futures and options contracts, are common ways to reduce risk. Private and public insurers are also developing new contracts for revenue, yield, and price insurance.

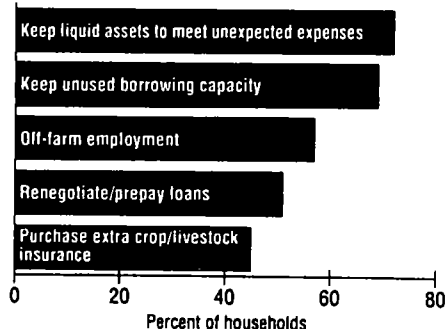
Although the 1996 act does not authorize a risk-management savings account program, it gives jurisdiction for any such program to USDA's new Risk Management Agency. Strong farm income from both high grain prices and the new transition payments encouraged such accounts to be proposed during the 1996 legislative session.

Risk Management Not New to Farm Households

Saving money for a rainy day forms the foundation of risk management accounts, but is certainly not new, especially for many farmers. Even though farm income typically varies more than a salary or hourly wage, farm household consumption actually varies relatively little. USDA surveys reveal that most farm households already use one or more existing techniques that may substitute for tax-deferred risk management accounts (fig. 1). At the extreme, some farmers would use accounts primarily to

Figure 1

Commercial farm households use many risk management techniques



Source: Compiled by Economic Research Service from Farm Costs and Returns Survey, 1994-95.

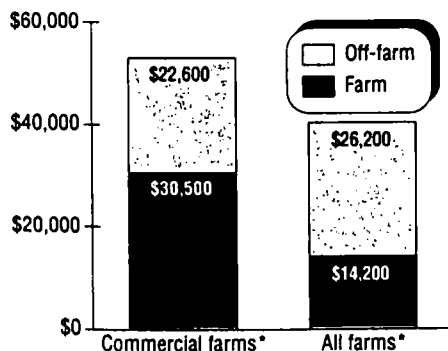
manage income tax liabilities, while others would be unable to benefit because of low taxable farm income.

Households respond to uncertainty by buying insurance, accumulating savings, reserving unused borrowing capacity, renegotiating or prepaying loans, and earning off-farm income. During years with low net income, farm households commonly delay the purchase of new capital equipment and "live off depreciation." That is, commercial farms (gross sales greater than \$50,000) often have several thousand dollars of depreciation charges annually. This noncash reduction from accounting income can easily be used in the short term to smooth household consumption or to pay other farm expenses. Many farm operators, even those who report farming as their major occupation, receive a substantial portion of their total income from off-farm sources, which provide a predictable component to household income (fig. 2).

Farm household consumption, however, may be more sensitive to declining Government payments than to an equal decline in farm income from prices or yields. Consumption from income varies greatly based on the source of income. Predictable sources of income are often spent more readily, while uncertain sources of income usually produce relatively

Figure 2

Commercial farm households average more total income but less off-farm income



*Reporting farming as major occupation.
Source: Compiled by Economic Research Service from Farm Costs and Returns Survey, 1995.

Canada's Experience

The Net Income Stabilization Account (NISA), a type of risk management account, is one component of Canada's farm safety net. Like proposals for tax-deferred risk management accounts in the United States, NISA is a farm-level risk management savings program. NISA, however, matches farmer deposits dollar for dollar with government contributions. It also adds a 3-percent interest rate subsidy on farmer contributions. Farmers make deposits with after-tax income, but government contributions and interest earnings are tax-deferred. They can deposit annually the smaller of \$5,000 or 2 percent of eligible farm sales. This limits the government match to \$5,000 per farmer. Farmers can also make additional nonmatched contributions of up to 20 percent of sales. Account balances may not exceed 150 percent of the farm's 5-year average sales. Withdrawals are allowed only when farm income falls below established thresholds.

Evidence from NISA suggests that most farmers deposit only enough money to earn the maximum matching government contribution. This suggests that the matching contribution is relatively more important than the interest rate subsidy and that similar saving behavior may be achieved by only partially matching the deposit. Observations also suggest that some farmers do not withdraw as much money as expected during low-income years. This indicates that many farmers prefer to manage income variability by other means rather than stop receiving government benefits on accumulated balances.

greater savings. Farm families, however, often consume off-farm income and Government payments at twice the rate of farm income.

Because household consumption is more sensitive to predictable Government payments than it is to uncertain farm income, reduced Government involvement may cause farm household consumption to vary more noticeably. Tax-deferred risk management accounts may eventually help reduce this variability if they promote greater saving.

Program Details Would Determine Level of Benefits and Their Distribution Among Farmers

Tax-deferred risk management accounts could be targeted to farmers based on transition payments or some measure of farm income. If farm income is the target, producers who were ineligible to receive program payments (for example, on livestock or specialty crops) under previous farm programs could nonetheless participate in tax-deferred risk management accounts.

Because the goal is to safeguard farm families from risks unique to agriculture, rules for deposits and withdrawals would likely be related to farm income. A practical method may tie program eligibility to common income tax measures, such as business capital gains and net farm income on Schedule F of Internal Revenue Service (IRS) Form 1040. This approach, however, would cause most of the benefits to be realized by established farmers with higher incomes.

If deposits into risk management accounts are limited to positive net farm income reported for taxes, many farmers will be unable to participate in the program because of insufficient income. Based on 1993 IRS data, which is fairly typical of other years, median farm net income reported for tax purposes was only \$11,300 for farmers who received more than half of their total taxable net income from farming. In fact, nearly one out of every five of these farmers reported a net farm loss for tax purposes, and another third had positive net farm income under \$10,000. Transition payments under the 1996 act, however,

may increase farm income above historical levels for some farmers.

In addition to defining the types of income that may be tax deferred, rules for qualified withdrawals are also important in determining program effects. If withdrawals are made at times other than low-income years, farmers could be assessed a penalty in addition to their deferred taxes because they would be using the fund for reasons other than managing risk. Economic definitions of low-income years may be difficult to implement on Schedule F. Commodity price triggers may be incorporated into tax forms, but would not necessarily reflect farm-level income variability. Historical averages of taxable farm profits might allow individual income testing, but may not reflect income or consumption variability targets. Farm income reported for taxes is different from other definitions of economic income because of accounting practices, such as prepaid expenses, deferred sales, accelerated depreciation, and capital expensing.

The Value of Tax Deferment May Be Large for Some. The value of tax deferment over a regular account can be quite large, especially if farmers can defer income until it can be taxed in a lower bracket upon withdrawal (fig. 3). The value of deferral increases further for people in the higher brackets. Because each of the five Federal income tax brackets covers a wide range of income, many farmers will be unable to reduce their bracket during high-income years. For example, deferring as much as \$5,000 of income would have reduced the marginal tax rate for only about one out of every five farmers in 1993. Many farmers may have too little income to save that much after paying living expenses.

Two factors increase the value of tax deferment over similar savings accounts, such as IRA's. Risk management accounts could defer self-employment taxes in addition to regular income taxes. Self-employment taxes may be a substantial part of a farmer's total tax

liability, depending on off-farm income. Farmers would also benefit during low-income years when withdrawals would allow them to use deductions or exemptions that would otherwise be lost if no tax were due. On the other hand, the value of tax deferral would be less than that associated with IRA's because the funds would typically be invested for a much shorter time.

Financial Incentives Affect Farm Management. Farmers do respond to tax incentives, as indicated by their widespread use of cash accounting tax laws to defer income and capital expensing to reduce the cost of equipment purchases. Tax incentives seem to have less effect on saving behavior, however; only 12 percent of farmers contributed to tax-deferred retirement accounts in 1993. Risk management accounts may attract more savers, though, because funds could be withdrawn from such accounts during low-income years.

Because tax-deferred accounts transfer income and taxes across time, they share similarities to income tax averaging. Risk management accounts, however, may be more powerful because they can defer taxes for many

more years than allowed by former or proposed income tax averaging rules.

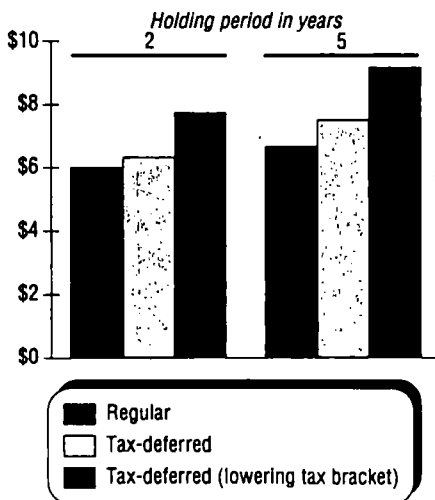
Any type of risk protection can create moral hazards. For example, farmers might buy less insurance, manage with less diligence, or not diversify or rotate crops. Risk management accounts may cause relatively smaller moral hazards, however, because of the self-insurance nature of the program. Income stabilization is possible only when balances have been accumulated out of the farmer's own profits. Those profits and balances are directly at risk if poor management develops. Nonetheless, farmers in regions with more production variability or with less diversification would stand to benefit more than producers with less income variability.

Direct subsidies are usually preferable to indirect subsidies because they do not distort economic decisionmaking as much. Tax incentives are less distorting than acreage, loan, and deficiency payment provisions of previous farm acts, but are more distorting than the transition payments under the 1996 act. Given Federal budget pressures and objectives of the 1996 act, targeted tax incentives seem the most likely way such accounts would be subsidized, rather than with more direct Federal outlays such as interest rate subsidies or matching Government contributions.

Another difficult question arises from balances remaining in tax-advantaged accounts when the farmer retires. Converting the funds from risk management into a retirement account ignores the original targeting objective. Abuse may be limited by placing ceilings on deposits and balances that reflect reasonable amounts to cover basic living expenses for 2 or 3 consecutive low-income years. A more aggressive approach may be to require accounts to be liquidated and fully taxed when the taxpayer stops farming. By comparison, legislation passed in 1996 for medical savings accounts allows balances to be converted into retirement use after age 65 without additional penalties.

Figure 3

Future value of account balances with and without tax-deferral, by account type



Note: Assumes \$10 of pretax self-employed income; 28-percent marginal Federal tax, self-employment tax, and 3-percent State tax; and 5-percent rate of return.
Source: Compiled by Economic Research Service.

Small Effect on Rural Economies Likely

Beyond the farm gate, other groups may be affected by risk management accounts. If household consumption in the past was smoothed by delaying the purchase of certain items, merchants in rural communities may benefit from more stable sales. In the short term, however, some farmers may delay capital or consumption purchases while they build their reserve fund. Widespread use of risk management accounts may also result in less reinvestment in agricultural assets and a greater allocation to off-farm investments. The net effect would be small compared with the total amount of farm investment.

The aggregate effect on farmers' consumption and investment decisions will also depend on future expectations about Government programs. If farmers believe program benefits will be transitory, they will tend to consume less of that income than if future payments are believed to be permanent and reliable. Consequently, risk management accounts may be more actively used if long-term consumption and investments are reduced because of these expectations.

Rural economies are more likely to benefit from the potential for smoother consumption than from additional incentives to save. Integrated capital markets may channel additional savings out of the local community. More predictable farm household consumption will provide only limited benefits to rural economies because of the decreasing importance of farm income relative to other sources of income.

Conclusions

Tax-deferred risk management accounts could offer a unique potential for farmers to self-insure part of their income risk. Many issues, however, confront policymakers: tax accounting and targeting issues, the potential for long-term tax avoidance or retirement savings, the proportion of farmers who would use them, and the concentration of benefits to more prosperous farmers.

Tax advantages of risk management savings accounts are clear, especially for farmers who, by participating, could avoid higher marginal tax brackets in high-income years or more fully use tax deductions by taking withdrawals in low-income years. Many farms with low net income, however, may be kept from sharing in these benefits because of restrictions targeting farm income.

Most farm households are already able to smooth consumption by earning off-farm income, delaying capital purchases or principal repayments, using additional short-term borrowing, and drawing cash flow from depreciation expenses. Risk management accounts may help educate farm households about the value of saving and serve as another useful management tool. But, such accounts may also encourage farm households to shift currently taxable savings to tax-sheltered savings or to substitute saving for other consumption-smoothing techniques. These effects are likely to dominate farm household behavior. Thus, additional benefits to rural economies would be relatively small. Finally, tax incentives for risk management savings accounts are not likely to significantly reduce the demand for special disaster relief from the Federal Government.

Contacting the Author

James Monke
(202) 219-0343 (voice)
(202) 219-0908 (fax)
e-mail: JMONKE@ECON.AG.GOV

Further Readings

Chen, Kevin, and Karl Meilke. "A Reevaluation of Canada's Safety Net Programs for Agriculture." *Canadian Journal of Agricultural Economics*. Dec. 1996.

Coble, Keith. "Canada's NISA Program: A Strategy for Stabilizing Farm Incomes." *Agricultural Outlook*. USDA/ERS. May 1995.

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The Value and Role of Public Investment in Agricultural Research

May 1995



United States Department of Agriculture
Economic Research Service

The Value and Role of Public Investment in Agricultural Research. Keith Fuglie, Nicole Ballenger, Kelly Day, Cassandra Klotz, John Reilly, and Jet Yee. Natural Resources and Environment Division, Economic Research Service, U.S. Department of Agriculture, Washington, DC. Staff Paper No. AGES-9510.

Abstract

This document outlines, in graphs and figures, ERS research findings about funding trends, rates of return, and public-private collaboration in agricultural research. This document was prepared as background for a briefing of the Under Secretary for Research, Education, and Economics of the United States Department of Agriculture.

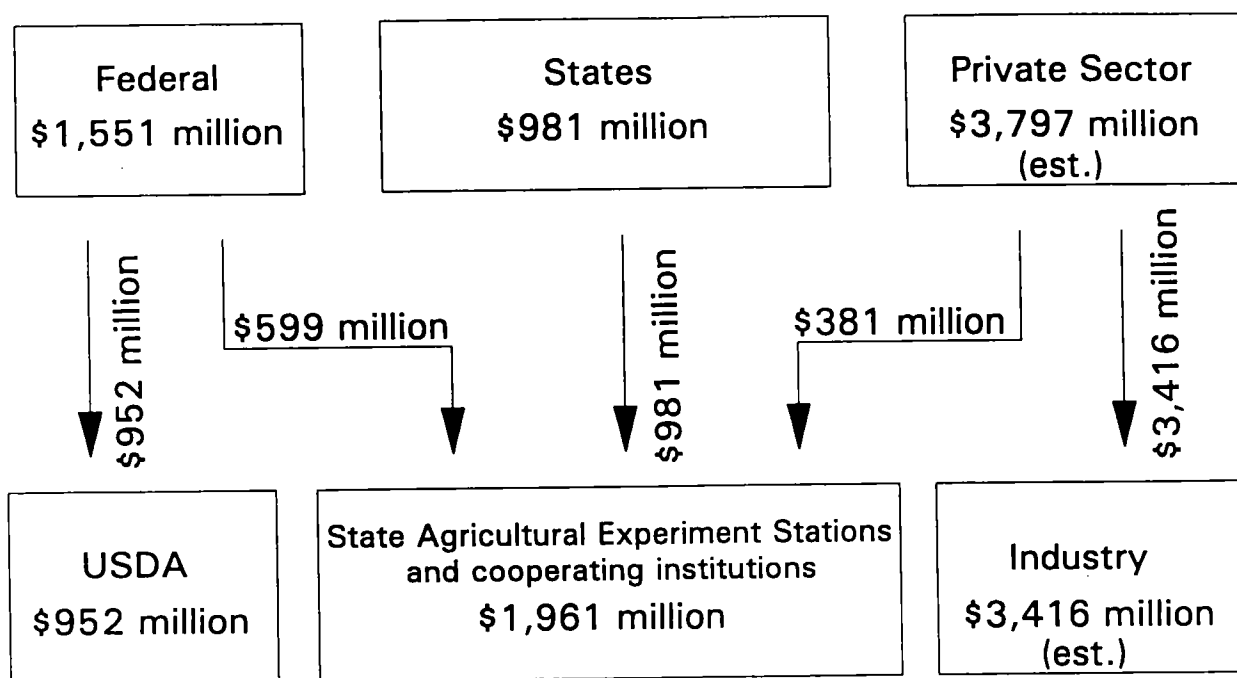
Keywords: United States, agricultural research, rate of return to research, economics, public-private collaboration in research, intellectual property rights.

Acknowledgments

This material draws upon research of the Natural Resources and Environment Division's (NRED) program on **Research, Development and Technology Policy Analysis**. The authors thank Robbin Shoemaker, George Frisvold, Ian Parry, and Bob Robinson for their useful comments and suggestions.

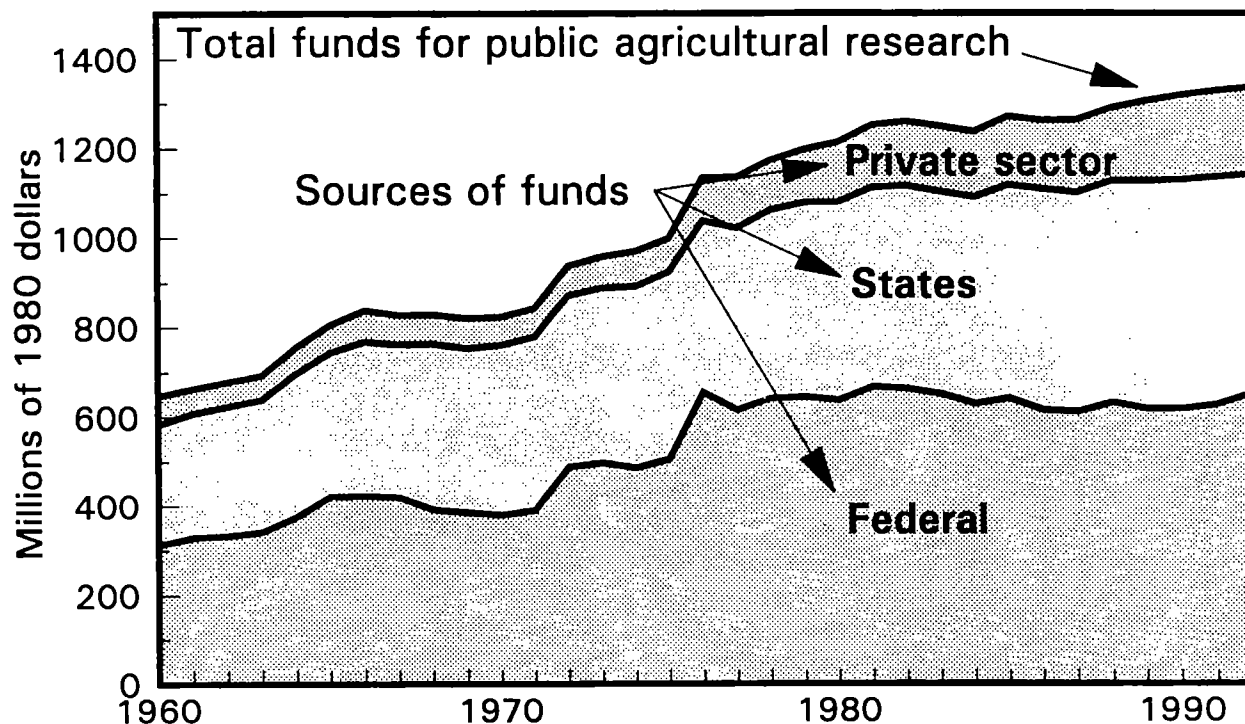
Agricultural Research in the U.S. is Shared Responsibility

Flow of funding in 1992



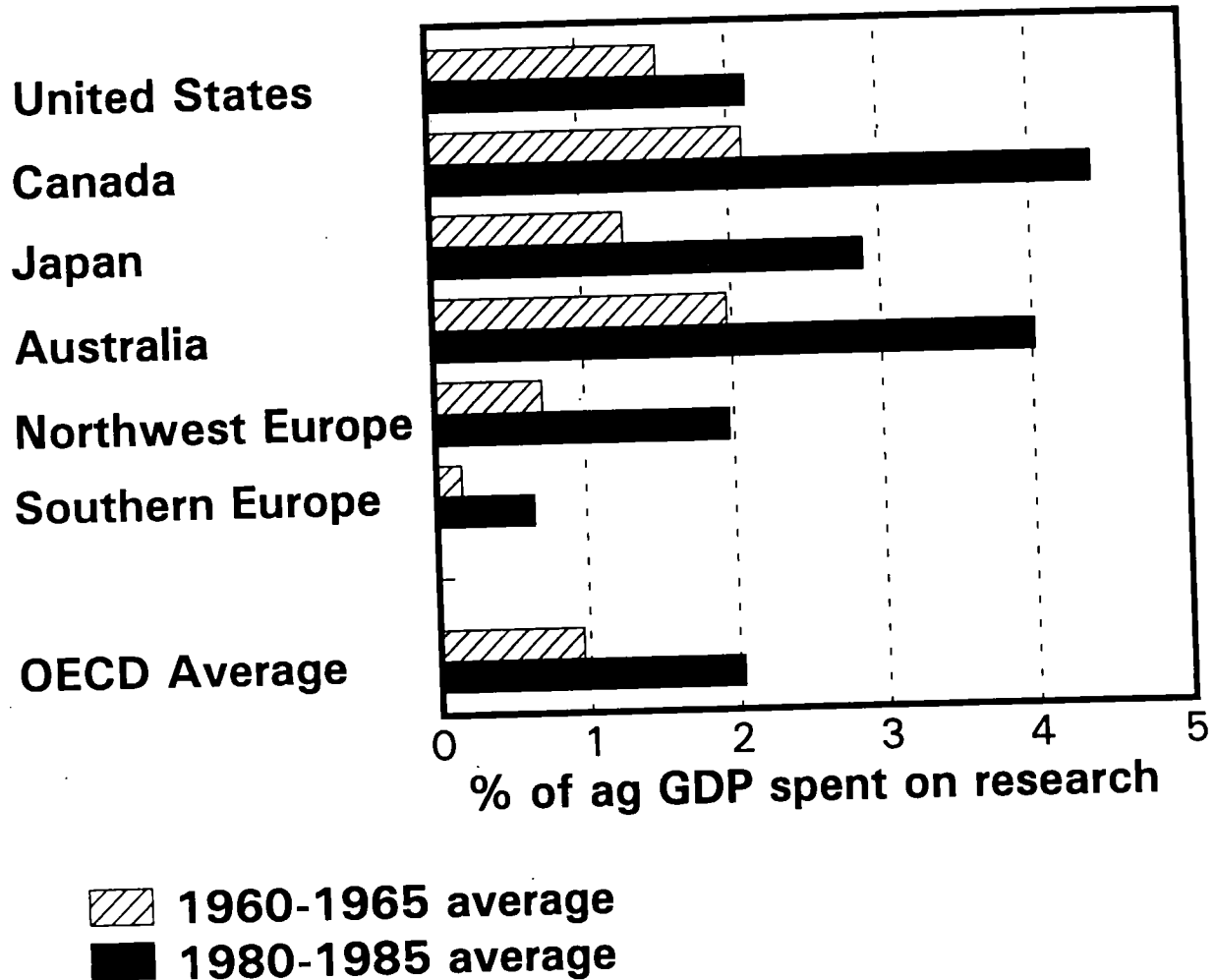
- △ Technical advance in U.S. agriculture is a shared responsibility between the public and private sectors. Public research is conducted by a system of Federal and State research institutions, with the Federal government providing more than half of the financial support for this system. Of the Federal money going to State Agricultural Experiment Stations, about 60% is administered by the USDA, with the rest coming from other Federal agencies.
- △ The figures for private spending for food and agricultural research are only estimates, and are probably low.

Federal Funds for Agricultural Research Stagnant Since 1976



- △ The figure shows trends in expenditures by the public agricultural research system after adjusting for inflation in the cost of conducting research. Research costs have been rising faster than the rate of inflation by about 0.4% per year since 1960.
- △ Public agricultural research expenditures grew in real (inflation-adjusted) terms by 3-4% per year before 1980, but growth has slowed to less than 1% per year since then. Most of the current growth comes from increased contributions from the private sector to State Agricultural Experiment Stations. Federal support for agricultural research, which includes both intramural research at USDA research agencies and Federal money for State institutions, has been stagnant since 1976. State governments continued to increase real spending for agricultural research until the economic recession of the early 1990's.

U.S. Agricultural Research Losing Ground Relative to OECD Countries



△ Public support for agricultural research in the U.S. has been losing ground relative to other OECD countries. As a percentage of agricultural GDP, or the value of all goods and services produced in agriculture, the U.S. was above the OECD average in the early 1960's, but fell to about average by the early 1980's. This occurred despite the fact that U.S. spending on research increased from about 1.5% to just over 2% of agricultural GDP over this period. In the 1980's, two of our major competitors in international grain markets, Canada and Australia, were spending about twice as much as the U.S. on research relative to the size of their agricultural economies.

Returns to Agricultural Research High

Economic studies have estimated high returns to public agricultural research

Estimates of the rate of return have generally been around 40-60%. These estimates are based on the total benefits from new technology to the economy, including benefits to farmers, agribusinesses, and consumers.

Estimates may be biased upward

Critics have identified five broad factors that may bias the estimated rate of return. (1) Some studies did not account for the contributions of the private sector to developing and disseminating new technology. (2) Raising tax revenues gives rise to market distortions known as "deadweight losses." Economists have estimated that one dollar in public spending may have an economic cost of around \$1.30. (3) The estimates of the returns to research are sensitive to assumptions made about the time lag between when research is conducted and when new technology is finally adopted by farmers. (4) New technology may only serve to increase surpluses and exacerbate commodity program costs. And (5), these estimates have not taken into account the costs of new technology to the environment, to human health, and to resource adjustments, such as the exit of labor from agriculture.

Conservative estimate still shows high return

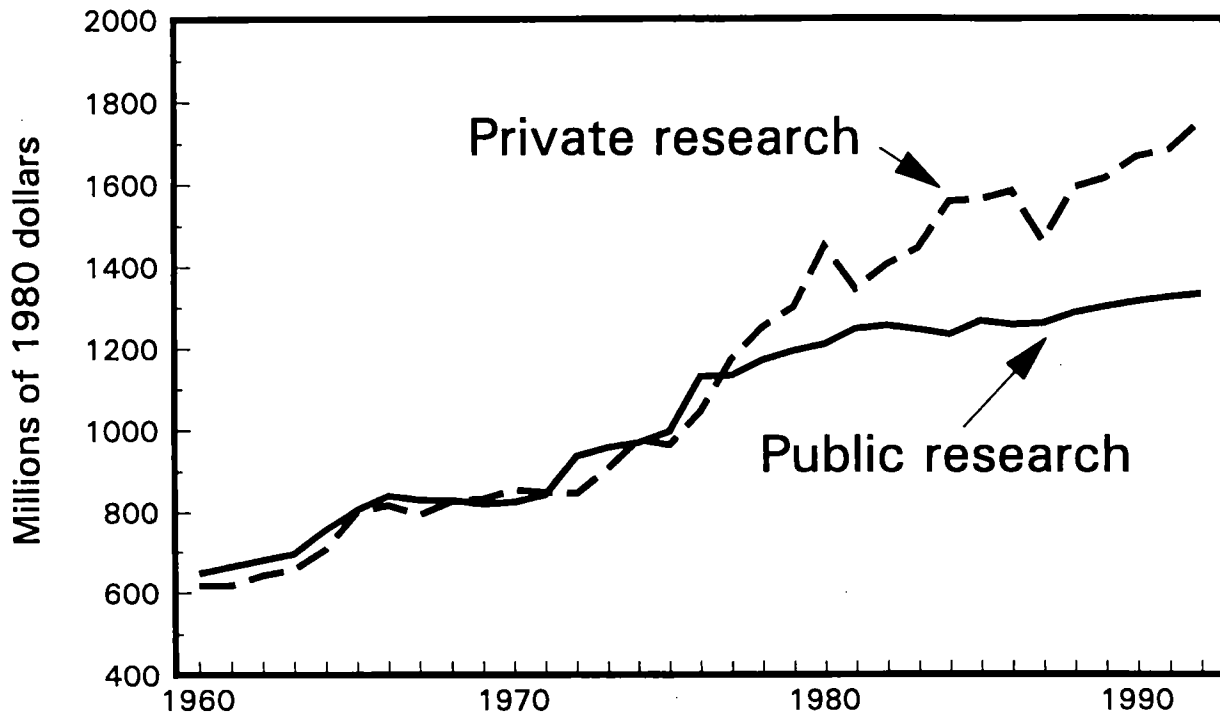
Recent work at ERS has reevaluated the returns to agricultural research in light of these factors. This analysis took into account the full economic cost of public expenditures, costs incurred by the private sector in technology development, and used conservative assumptions about the research lag. These factors reduced the estimated rate of return from 60% to 35%. The effects of increased production on commodity programs appear not to have been significant over the long run, due to periodic adjustments in price supports that kept program costs from rising in real terms. The effects of new technology on the environment, on human health, and on resource adjustments are not well understood at the present time. However, the net effect of these factors may not necessarily be negative. For example, new technology that increases yields reduces the need to expand production into environmentally sensitive areas. Labor that exits agriculture may eventually find higher-paying non-farm jobs.

With these limitations, it appears that even under conservative assumptions the rate of return to agricultural research in the U.S. has still been quite high, probably at least 35%.

● Implies underinvestment in agricultural research

A high rate of return means that many beneficial projects are not being funded.

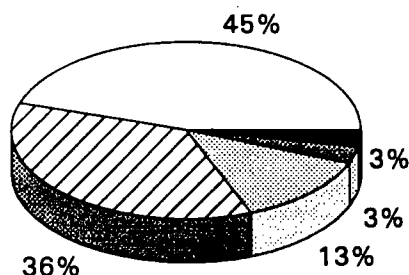
Private Agricultural Research Growing



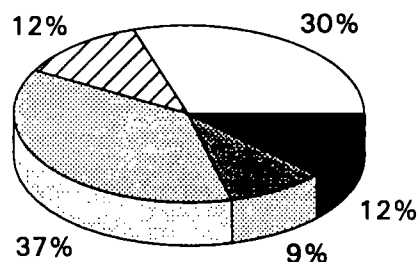
Annual expenditures adjusted for inflation by cost-of-research index

- △ One of the major trends in agricultural research in the U.S. has been the growing role of the private sector in providing new technology to farmers. In real terms, private expenditures for food and agricultural research tripled between 1960 and 1992. Total expenditures by the private sector surpassed spending by the public system in the 1970's if not earlier. The estimates of private spending for agricultural research are incomplete, because much of this information is not publicly available. Actual yearly spending by the private sector may be several hundred million dollars higher than shown in the figure.

Private Research Moving Into New Areas



1960: \$206 million



1992: \$3,416 million

Food products
 Farm machinery
 Farm chemicals
 Animal health
 Plant breeding

- △ In the past several decades, private agricultural research has moved aggressively into new areas, such as plant breeding. In 1960, the division of labor between the public and private sectors was fairly clear. At that time, about 80% of private research was spent on either developing new food products or farm machinery. Only about 20% was for technology to increase crop or livestock yields (farm chemicals, animal health, and plant breeding, in the figures). Yield-increasing technology was largely supplied by the public sector. By 1992, however, about 60% of private research was also devoted to developing yield-increasing technology. The growth in private spending for plant breeding has been particularly rapid during the past two decades.
- △ These trends suggest that there is more potential for overlap and duplication between public and private agricultural research today than was true in the past. It implies that greater coordination is needed between public and private research so that public research does not "crowd out" private research, and so that the two systems complement, rather than compete with, each other.

Incentives for Private Research

Increased demand for agricultural innovations

Worldwide food demand continues to increase with population growth.

New opportunities in biotechnology

Expectations of new market opportunities attracted private firms, although the early promise has not been realized as quickly as expected.

New sources of capital from industry

Since the 1970's there has been increased interest in agriculture from chemical, petroleum, and pharmaceutical companies. New sources of venture capital for biotechnology have also become available.

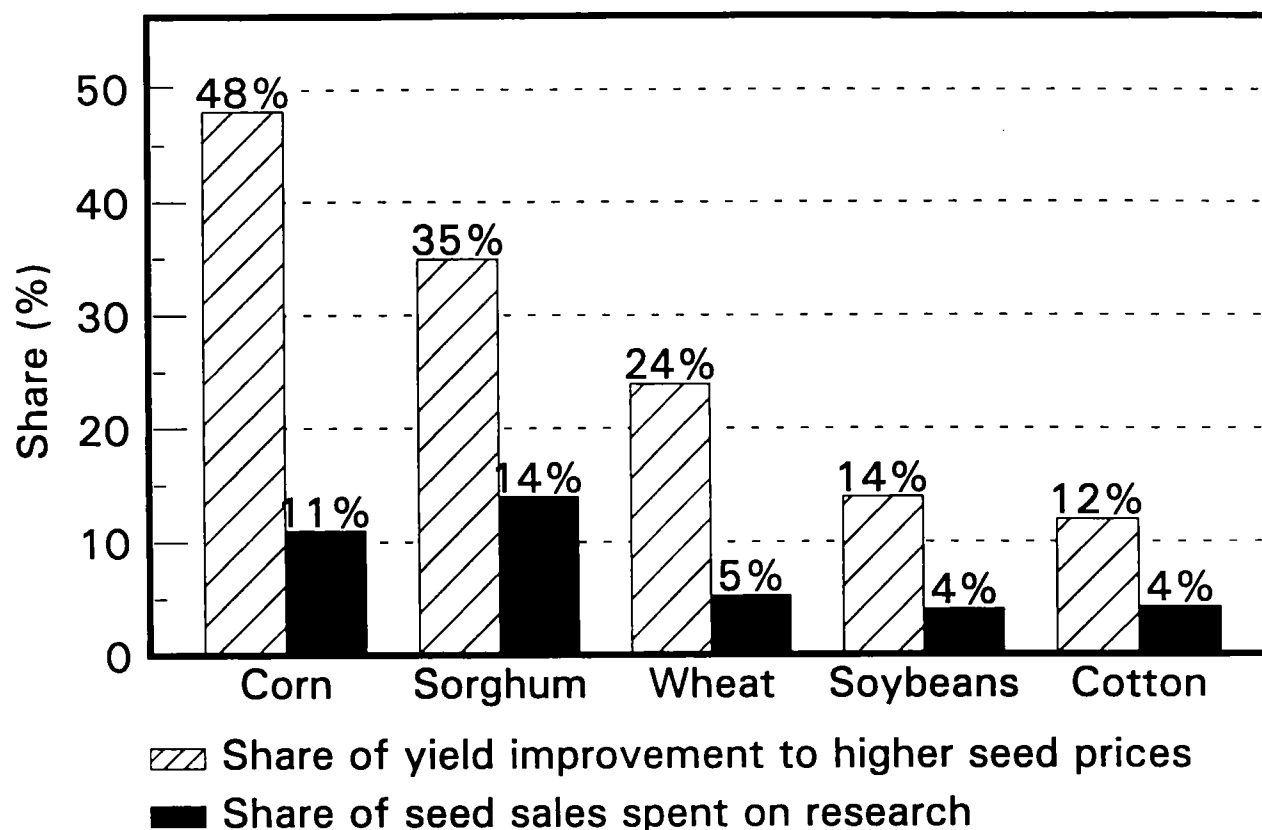
Strengthened intellectual property rights (IPR's) for biological inventions

The Plant Patent Act of 1930 and the Plant Variety Protection Act of 1970 established plant breeders' rights for new crop varieties. In the 1980's, judicial decisions established that genetically engineered plants and non-human animal life forms could also be patented.

IPR's: tradeoff between incentive to invent and monopoly power

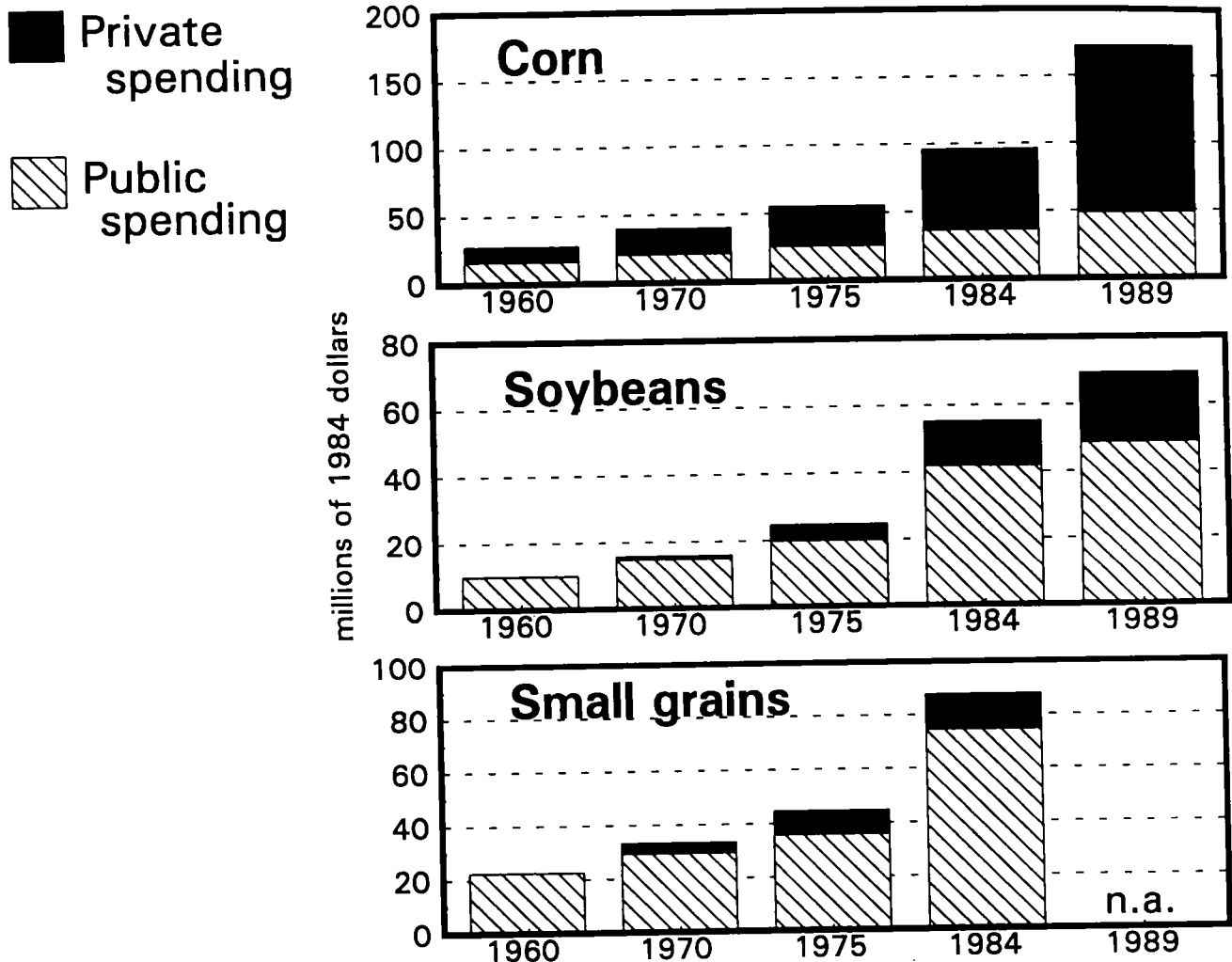
The strengthening of IPR's for biological inventions is controversial. On the one hand, they allow private firms to capture some of the gains from research and thereby increase their incentive to innovate. On the other hand, IPR's increase the market power of these companies and may restrict access to new technology by the scientific community. Public policy to strengthen IPR's involves a tradeoff between increasing research incentives and monopoly power.

Appropriating Gains from Research: Private Investment in Plant Breeding



△ This figure illustrates the relationship between private incentives and investment in plant breeding. For crops grown with hybrid seed, such as corn and sorghum, seed companies have been able to capture between one-third and one-half of the value of improved varieties by charging higher seed prices. In turn, they reinvest at least 10% of their seed sales in research. For crops grown from non-hybrid varieties, such as soybeans, cotton, and wheat, seed companies appear to be capturing less than one-fourth of the gains from plant breeding. Even though these varieties are protected by plant breeders' rights, private plant breeders cannot charge as high a price for them because of increased competition from seed companies that do not conduct research, and from farmers' own bin-run seed. As a result, only about 5% of the value of seed sales gets reinvested in research.

Public and Private Plant Breeding



△ When there is a strong incentive for the private sector to invest in research, there is less need for direct public funding. This figure shows the investment in plant breeding made by the public and private sectors for some important field crops. For corn, the private sector is able to appropriate a large share of the gains from plant breeding, and it spends over twice as much as the public sector. The character of public research on corn improvement has also changed with the growth of private investment in breeding. Public sector programs have moved to pre-technology research, such as corn genetics and enhancing the germplasm pool used by private breeders, and have left the development of finished varieties to the private sector. For non-hybrid crops such as soybeans and small grains, private incentives are weaker, and public breeding is still predominant.

Main Points

Federal support for agricultural research stagnant since 1976

Public agricultural research in U.S. was losing ground relative to other OECD countries through the mid-1980's

Returns to public agricultural research high ($> 35\%$)

Private agricultural research growing and moving into new areas

Needs and opportunities for public research

- basic research**
- applied research where private incentive low**
- collaborative research with private firms**

Comparative Advantage of Public Research

Basic research has highest return

The private sector lacks the incentive to conduct much of the research necessary to sustain productivity growth. This is probably clearest for basic, or pre-technology, research. Economic studies have found that basic agricultural research has about twice the benefit to society as more applied agricultural research.

Private sector lacks incentive to fund some types of applied research

If new technology cannot be packaged into a saleable product, the private sector is unlikely to develop it. Many new innovations in agriculture come in the form of information, such as improved management practices. Social science research, and research in support of public decision-making, are also unlikely to be supported by the private sector. Other areas where private incentives are low are for technologies that conserve natural resources, protect the environment, and enhance food safety and nutrition. These are areas where much of the benefits come in the form of non-market goods.

Private incentives low for some commodities

Incentives for private plant breeding appear to be good for hybrid crops, but are still fairly low for non-hybrid crops. To sustain yield growth for these crops, agricultural science policy can influence public research for plant breeding or increase incentives for private companies. In 1994, the Plant Variety Protection Act was amended to strengthen plant breeder's rights for non-hybrid varieties. These amendments prohibit farmers from reselling a portion of their crop as seed to other farmers, and also prevent other breeders from introducing small, cosmetic changes into a protected variety and then claiming it as a new variety.

Collaborative research: CRADA's and consortia

A mechanism for increasing the cooperation between public and private research is provided by the 1986 Technology Transfer Act. This Act set up guidelines for Cooperative Research and Development Agreements (CRADA's) between Federal laboratories and private industry. The USDA currently has over 200 active CRADA's with private firms.

Research consortia between Federal and state research institutions and groups of private companies can also be used to facilitate cooperation in research.

Risk Sharing Via Contracts Is Low, But Increasing For Field Crops

Output Under Production and Marketing Contracts

Commodity	1970	1994
Field Crops	2	8
Food grains	<1	13
Feed grains	11	20
Cotton		
Livestock	92	92
Broilers	60	65
Turkeys	95	95
Fluid grade milk	1	13
Hogs	18	11
Fed cattle		
Specialty Crops	85	88
Processed vegg.	21	25
Fresh vegg.	45	55
Potatoes	84	88
Citrus		

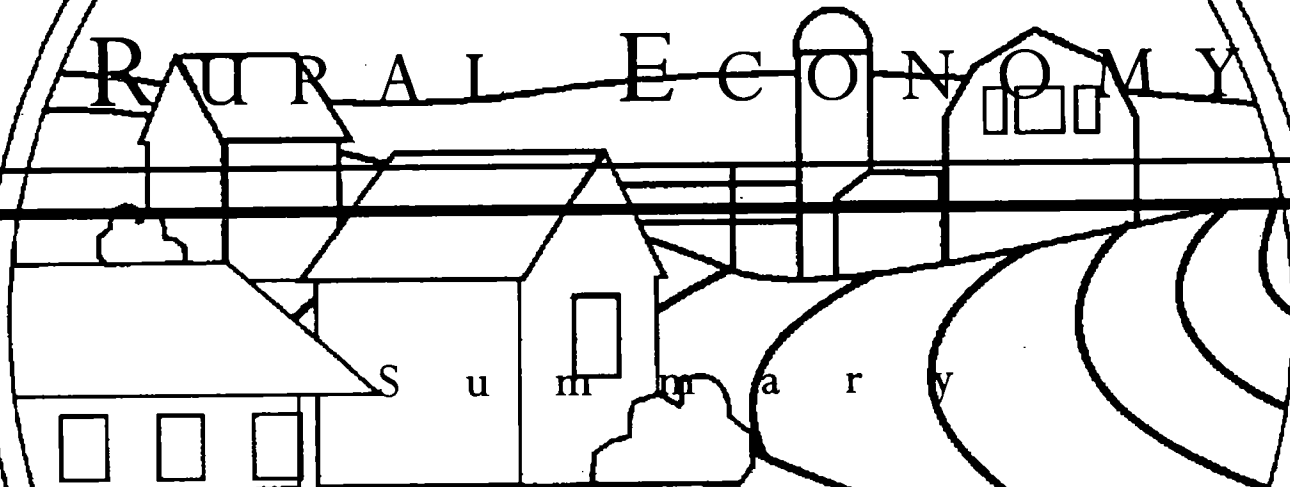
- The issue of price and income volatility and managing market risk goes beyond the farm gate to the food marketing system.
- Agribusiness has strong interest in dependable supplies, stable prices and constant margins rather than lower, but more volatile prices. Agribusiness is likely to join producers in search for risk management options.
- In food industries not covered by previous farm programs, such as livestock and horticultural products, risk sharing via production and marketing contracts has been a major risk management strategy.
- Output under production and marketing contracts for field crops is low, but increasing. FAIR could accelerate that trend in use of production and marketing contracts and other forms of "vertical coordination" for field crops.
- So, business strategies to reduce risk could have structural and vertical coordination implications.

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FARM STRUCTURE AND RURAL ECONOMY

FARM STRUCTURE AND RURAL ECONOMY

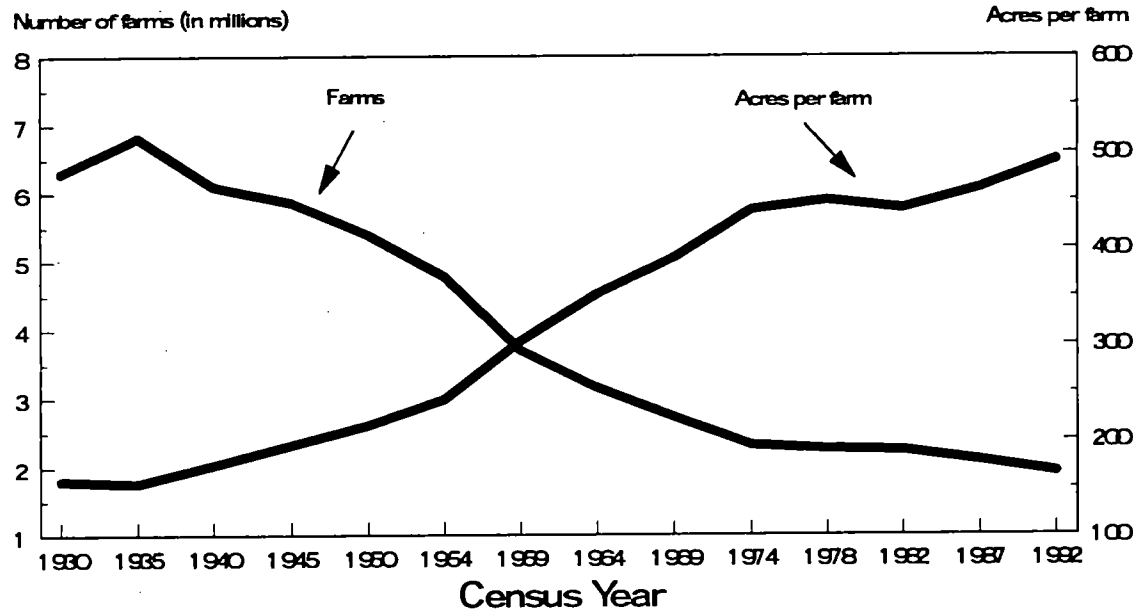


Farm numbers are expected to continue declining at about 2 percent a year for the rest of the decade, reaching 1.6 to 1.7 million by the year 2000. An increasing share of U.S. food and fiber is being produced on fewer farms, and farms have become more specialized.

Farm operator household income now equals that of all U.S. households. Farm households, on average, depend more on income from off-farm sources than from farming. Off-farm jobs are not necessarily in the food and fiber sector.

Natural resources (land, forests, water) are assuming new roles in the economy of many rural areas. The extractive value of natural resources is being eclipsed by the amenity value. Rural areas are increasingly viewed as desirable places in which to recreate, retire, and reside.

Farm Size Increased From 1930 to 1992 As Farm Numbers Declined From Their 1935 Peak



Prepared by the Rural Economy Division,
Economic Research Service, USDA,
using Census of Agriculture

Farm Numbers Will Continue to Decline

- Farm numbers have declined from the high of 6.5 million in 1935 to about 2 million today. Fewer farms implies larger farms since land in farms has remained near 1 billion acres over the period.

- Farm numbers declined the fastest during the 1950s and early 1960s. Mechanization allowed for the substitution of capital for labor, improving labor productivity and favoring farm consolidation to achieve lower per unit production costs. Low farm incomes, few nonfarm job opportuni-

ties in rural areas, and readily available higher paying jobs in urban areas led to major migration of hired workers, sharecroppers, tenants, and operators of small marginal farms to urban America. Fewer farm youth entered farming resulting in an aging of the farm operator population.

- The "seeds" of the "rural turn-around" that occurred in the 1970s were actually sown during the 1950s as manufacturing firms began to shift production facilities out of urban areas. While rural nonfarm jobs were expanding, this job growth was insufficient to absorb workers leaving farming.
- Expanding rural nonfarm job opportunities gained steam during the 1960s and 1970s mitigating the out migration by facilitating part time farming. Off-farm income eventually contributed to narrowing the income gap between farm and nonfarm households. Strong entry of young farmers during the boom years of the late 1970s stabilized farm numbers for a short time, but lower entry since the 1980s farm crisis continued the decline.
- Farm numbers are expected to decline by about 2 percent or less

annually for the rest of decade, reaching 1.6 to 1.7 million by 2000. The decline in farm numbers is not a threat to the Nation's food supply. Labor productivity on farms continues to increase. Younger farmers generally operate larger and more efficient farms than do older farmers whom they replace. Thus, fewer farmers can continue to produce the Nation's food and fiber.

Fewer Farms Will Produce Most Food and Fiber

- An increasing share of U.S. food and fiber is being produced on fewer and fewer farms. In 1940, 11.6 percent of all farms (689 thousand) accounted for one-half of all sales of agricultural commodities from U.S. farms. By 1992, the proportion had dropped to 3.2 percent (62 thousand farms). [Source: Census of Agriculture]

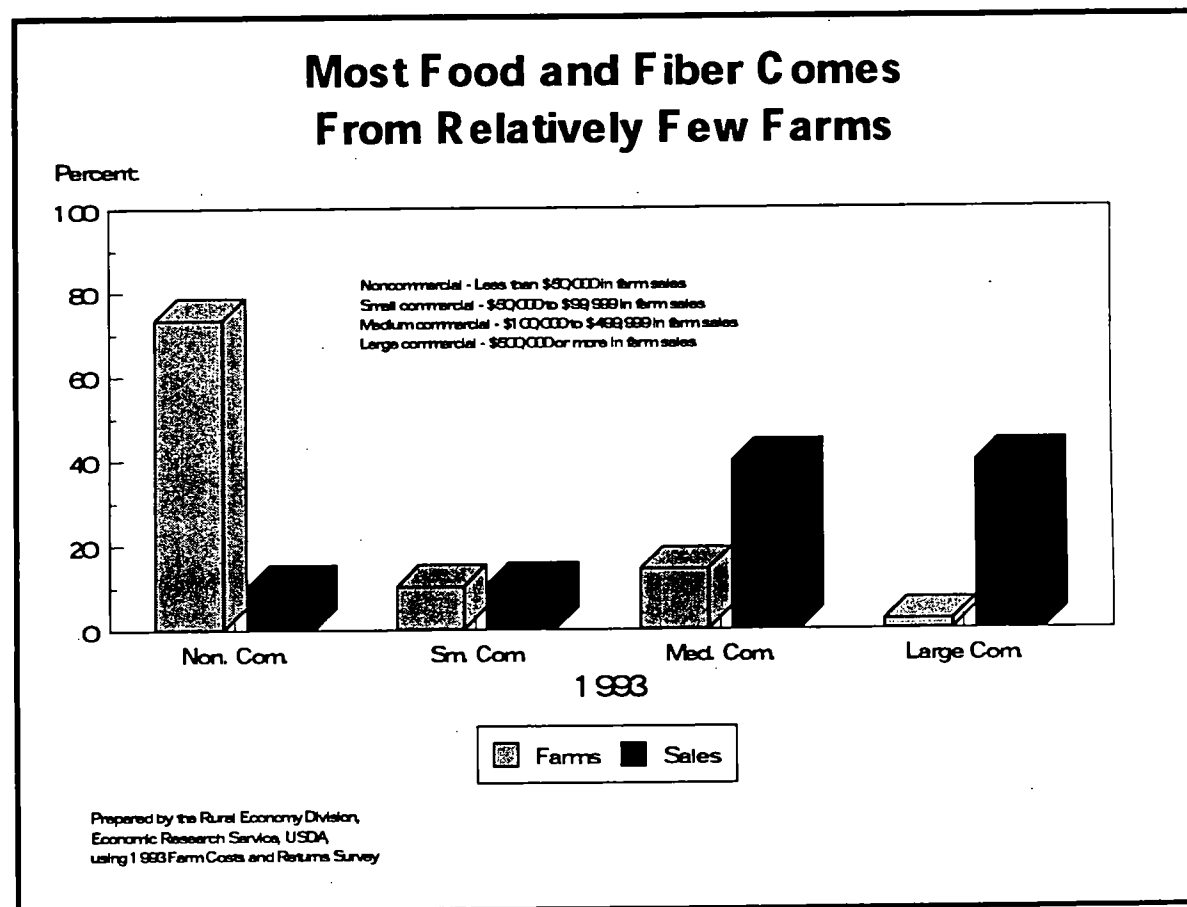
- A recent profile of U.S. farms shows that 73 percent of all farms reported sales of less than \$50,000. These non-commercial farms controlled 33 percent of all acres operated and 10 percent of total farm sales. In sharp contrast, about 39.6 percent of all sales came from 2.2

percent of farms. These large commercial farms have annual sales of \$500,000 or more. [Source: 1993 USDA Farm Costs and Returns Survey]

- The trend towards increasing concentration of production among fewer farms is expected to continue into the 21st century. Large commercial farms are expected to increase in

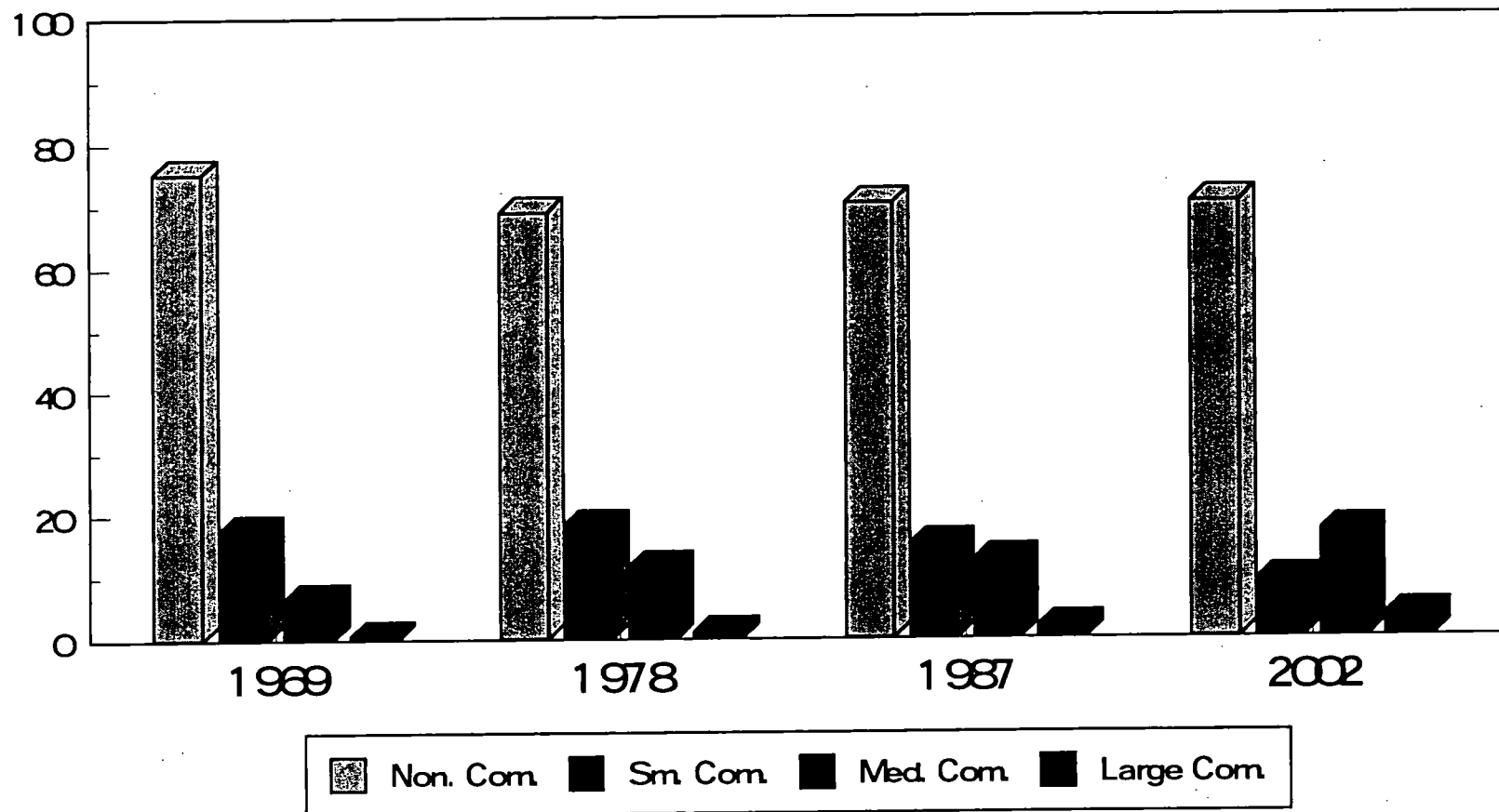
number and will likely be 3.5 percent of all farms by the end of the decade. The number of small commercial farms is expected to decline. Still, the farm sector is much less concentrated than are other sectors of the U.S. economy.

- While smaller farms are becoming less significant as producers of food and fiber, they are still important



Large Commercial Farms Expected to Increase

Percent of Farms



Prepared by the Rural Economy Division,
Economic Research Service, USDA

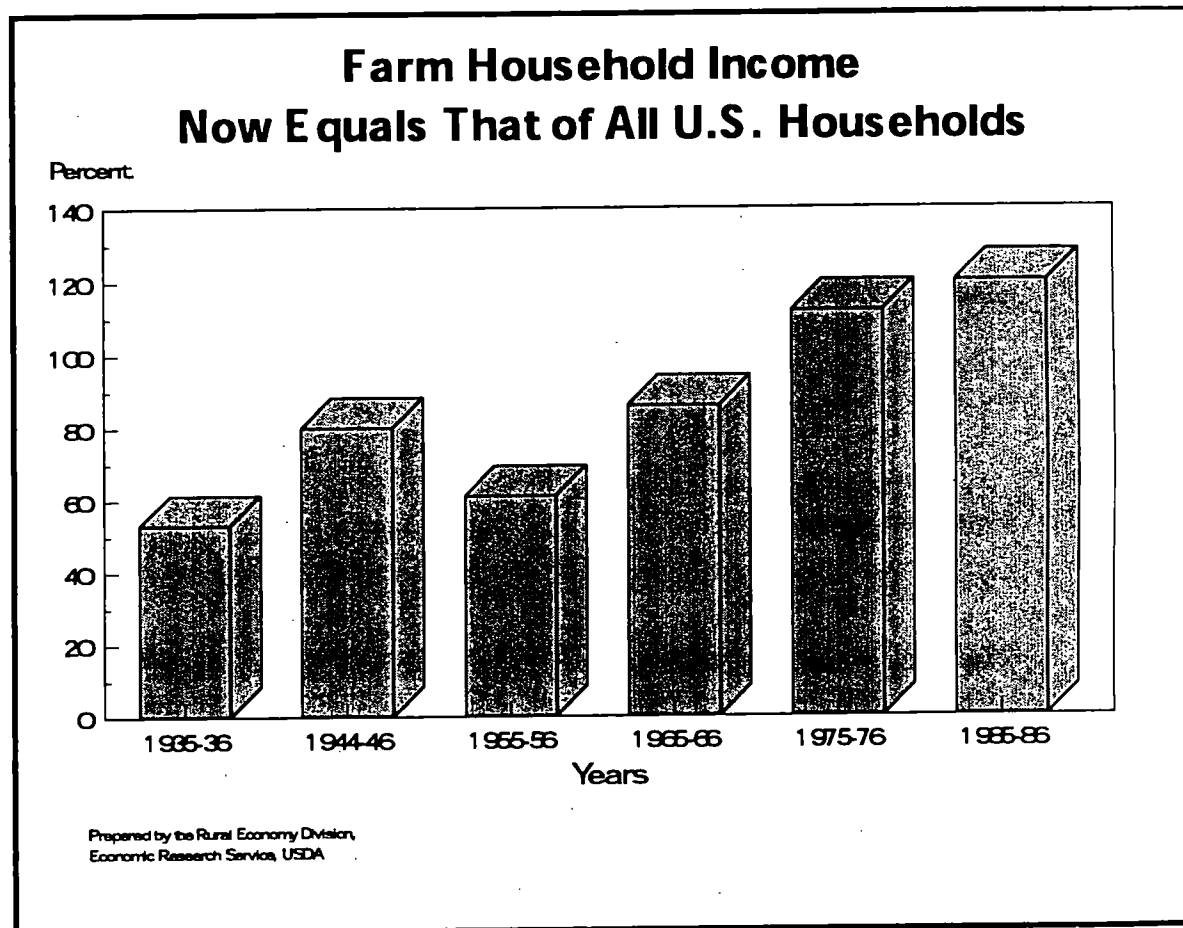
players in environmental and land use policies because they control a major share of U.S. farmland.

Farm Household Income Matches National Average

- Farm commodity programs were developed during a time when the average income of a farm households was about one-half that of all U.S. households. About 30 million people lived on farms in 1930, 24 percent of the total U.S. population and 56 percent of the rural population. Thus, efforts to raise farm family incomes would help ameliorate both U.S. and rural poverty.

- With the possible exception of the World War II period, this low relative income status persisted well into the 1960s. Farm households generally achieved income parity with all U.S. households during the 1970s and have remained that way, except for the early 1980s, ever since. Yet the general perception that farm families are relatively poor persists to this day.

- Improved access to rural non-farm jobs and income has played an important role in farm households achieving income parity. Farm house-



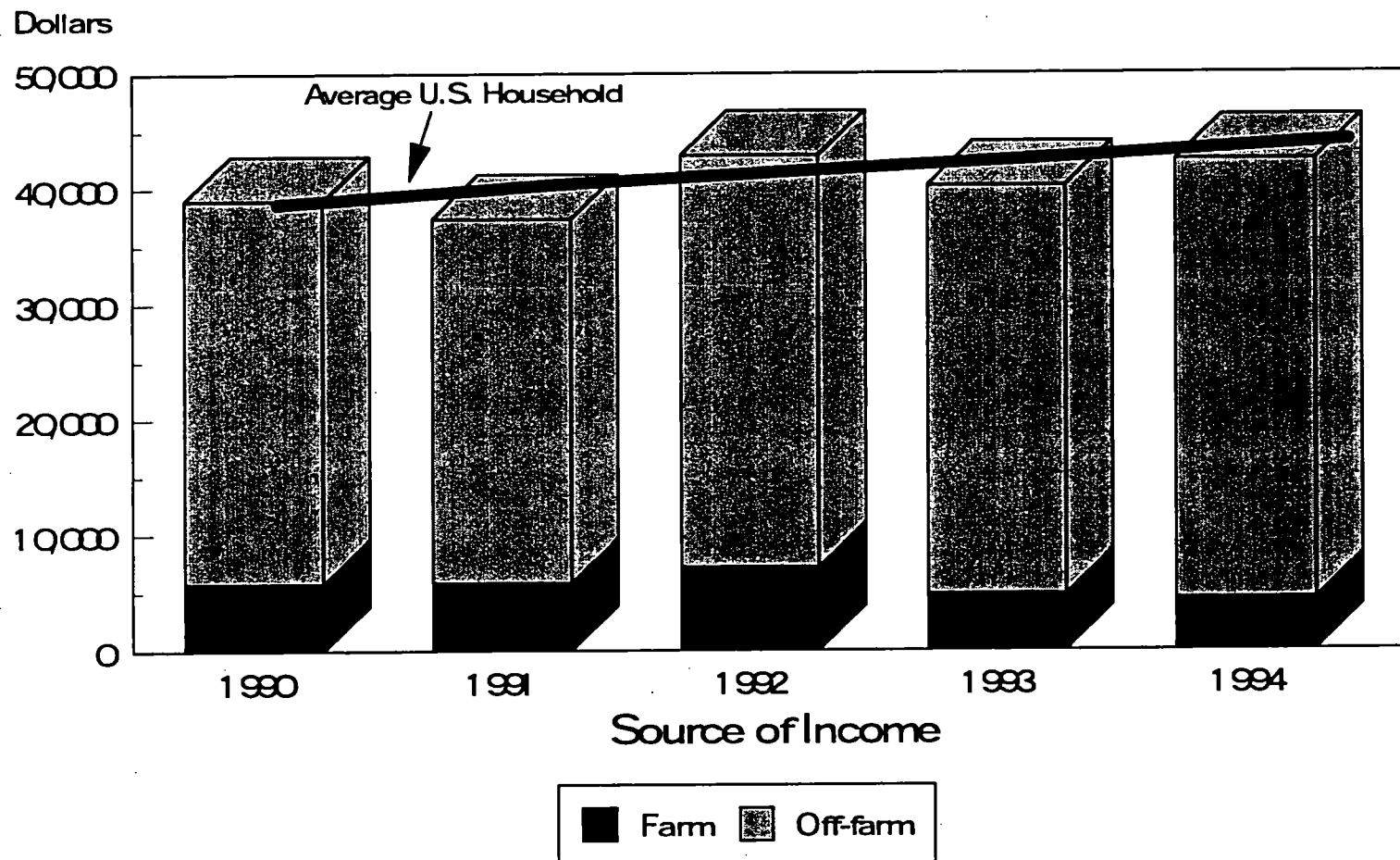
holds, on average, depend more on income from off-farm sources for family living than on income from farming. Farm households are not unlike the growing number of all U.S. households with two or more earners.

- The level and sources of household income vary by size of farm. Non-commercial farms depend exclusively on off-farm income as their farms

typically lose money. Farm households operating very large farms report relatively high incomes, most of which comes from farming. The off-farm income of these households is also not dissimilar to that of most nonfarm households.

- The net worth of farm households exceeds that of all U.S. house-

Farm Operator Households and U.S. Households Have Similar Income Levels



Prepared by the Rural Economy Division,
Economic Research Service, USDA
using Farm Cost and Returns Survey and Current Population Survey

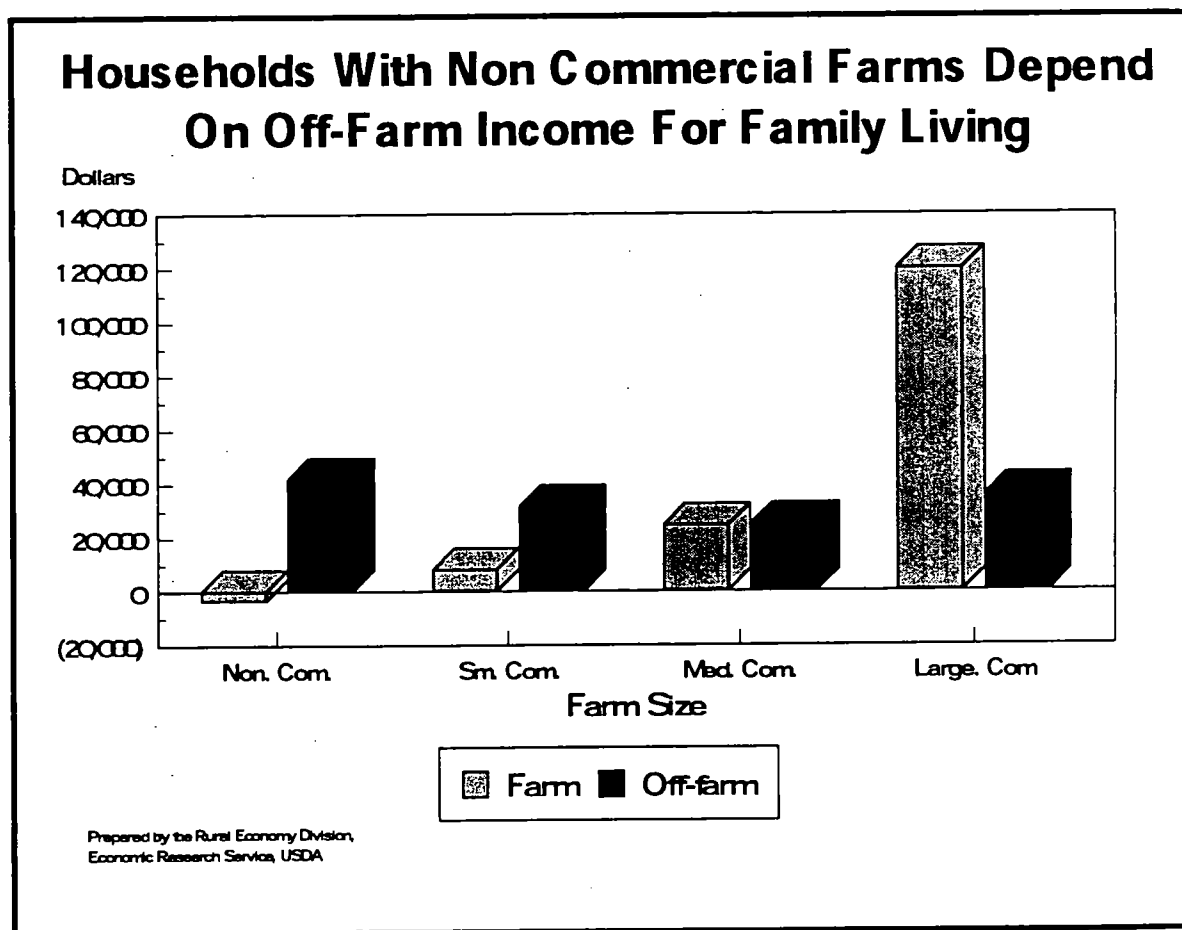
holds. (\$334,900 for farm households versus \$99,800 for all U.S. households in 1993.) But farming is a capital intensive business which requires substantial assets in order to generate average U.S. household income.

Food and fiber System Is Also Undergoing Structural Change

- There are about 21 million jobs in the U.S. economy (16 percent of all jobs) that involve growing, processing, and marketing the food that is consumed in the United States, exported to other countries, or imported from other countries. Jobs in farm production, agricultural inputs, and processing and marketing have declined in recent years. Job growth has occurred in wholesale/retail trade, the component of the system that is closest to the consumer.

- The number of food processing and food retailing establishments has declined over the last 30 years but the number of restaurants has increased. This reflects consumers' increasing desire to eat away from home.

- Food processing establishments are increasing in size. The share of

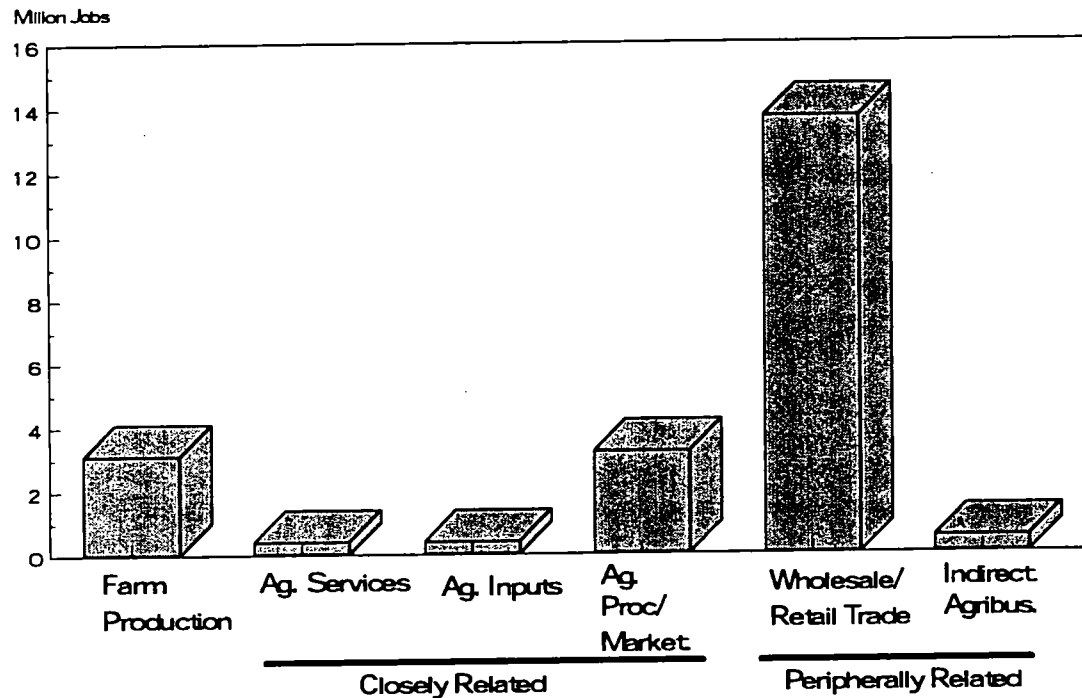


output supplied by all food processing plants with at least 500 employees increased from 28 percent in 1982 to 33 percent in 1992. Aggregate concentration is also increasing in the food processing industry. The share of sales accounted for by the top 20 firms increased from 23 percent in 1967 to 40 percent in 1987. But concentration varies widely among specific food

processing industries. For example, the largest 4 firms account for only 24 percent of shipments in the ice cream and frozen desserts industry, while the top 4 firms in the cereal breakfast foods industry account for 85 percent of shipments.

- In food retailing, supermarkets now account for 76 percent of grocery

Farm and Farm-Related Employment, 1992



Prepared by the Rural Economy Division,
Economic Research Service, USDA

store sales, up from 59 percent in 1963. Even within the supermarket category, there has been a rapid shift to larger stores. Since 1980, the average size of supermarkets has increased from 23,000 to 35,000 square feet. Aggregate concentration in food retailing has been rising at a moderate rate. The share of sales accounted for by the top 20 food retailing firms in-

creased from 34 percent in 1967 to 37 percent in 1987.

Farming No Longer Dominates Rural Economy

- The composition of the rural economy has changed since the

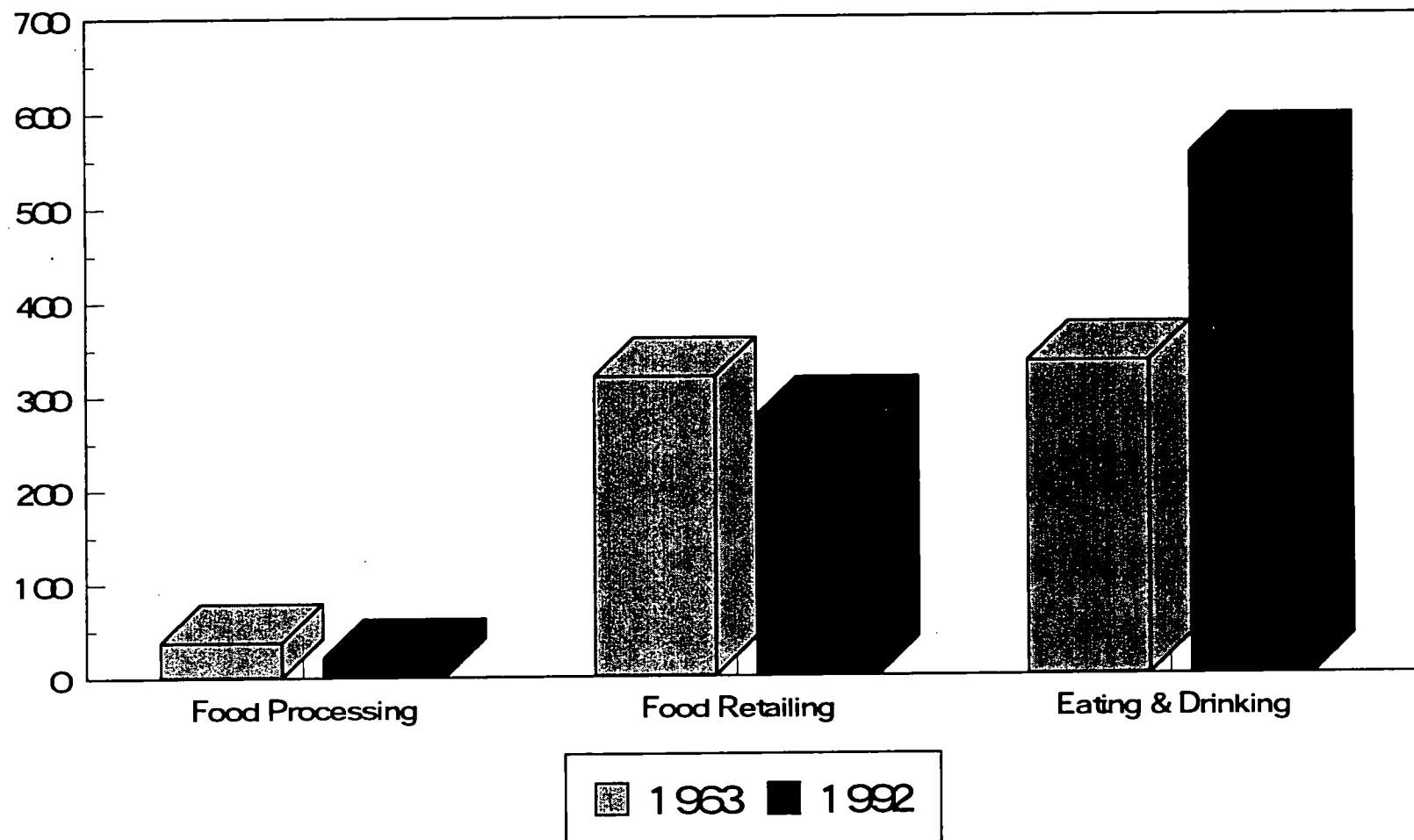
inception of agricultural programs. Farming no longer dominates. This change can be illustrated in a variety of ways. In 1950, farming contributed 20 percent or more of total county earned income in over 2,000 U.S. counties. By the late 1980's, only 556 depended on farming for this level of earnings. These counties are geographically concentrated in the western Corn Belt and Plains States.

- Today's rural economies are more likely to be dominated by manufacturing, services, or government jobs than by jobs in farming. While farming provided over 14 percent of all rural jobs in 1969, that proportion dropped to about 7 percent by 1993. Recent job growth has occurred in the services sectors of the rural economy. Retirement and recreation activities are particular economic bright spots in the rural landscape. Many rural counties serve as residential areas for workers who commute to jobs in other counties.

- Nor are rural jobs associated with the food and fiber sector, those industries associated with processing and marketing farm commodities or providing inputs to farm production. Only about 20 to 23 percent of rural jobs are associated with the food and

Changes in Number of Establishments, 1963-92

1,000 Units



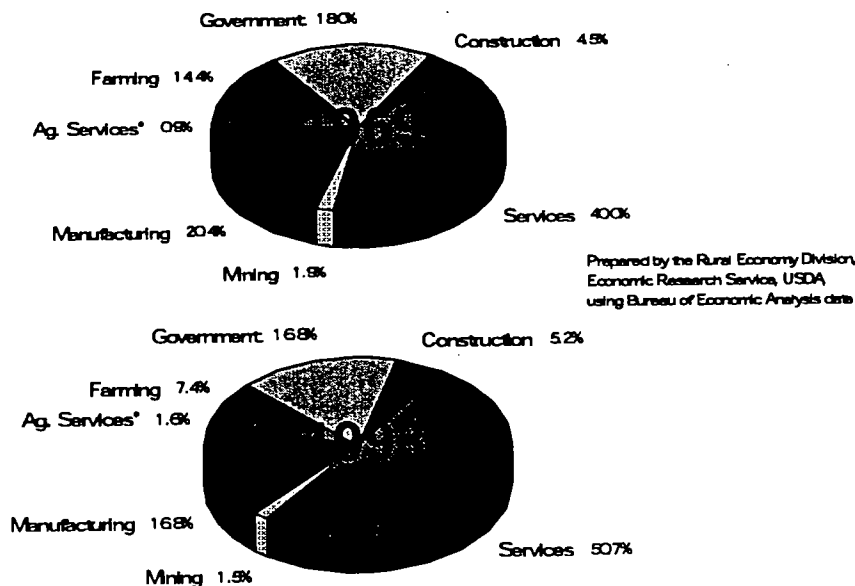
Prepared by the Rural Economy Division,
Economic Research Service, USDA

fiber sector. With the exception of farming, food and fiber sector jobs are more likely to be located in U.S. metropolitan areas, particularly jobs in wholesale and retail trade.

- Rural and small town areas exhibited a broad revival of population growth during the first half of the 1990's. Rural population rose 5.1

percent during 1990-95, nearly twice the rate of growth during the 1980's. About 1.3 million more people moved from metro America into rural and small town areas than moved in the opposite way -- a direction of net population flow contrary to that of any other time in the 20th century except for the 1970s and possibly the first half of the 1930s. During the 1980s, the net

Nonmetro Employment by Industry: 1969-1993



Suggested readings on characteristics of rural America...

USDA, Economic Research Service.
Understanding Rural America, Agriculture Information Bulletin 710, February 1995.

USDA, Economic Research Service.
Credit in Rural America, Agricultural Economic Report 749, April 1997.

...or visit the ERS Home Page briefing rooms on the following topics:

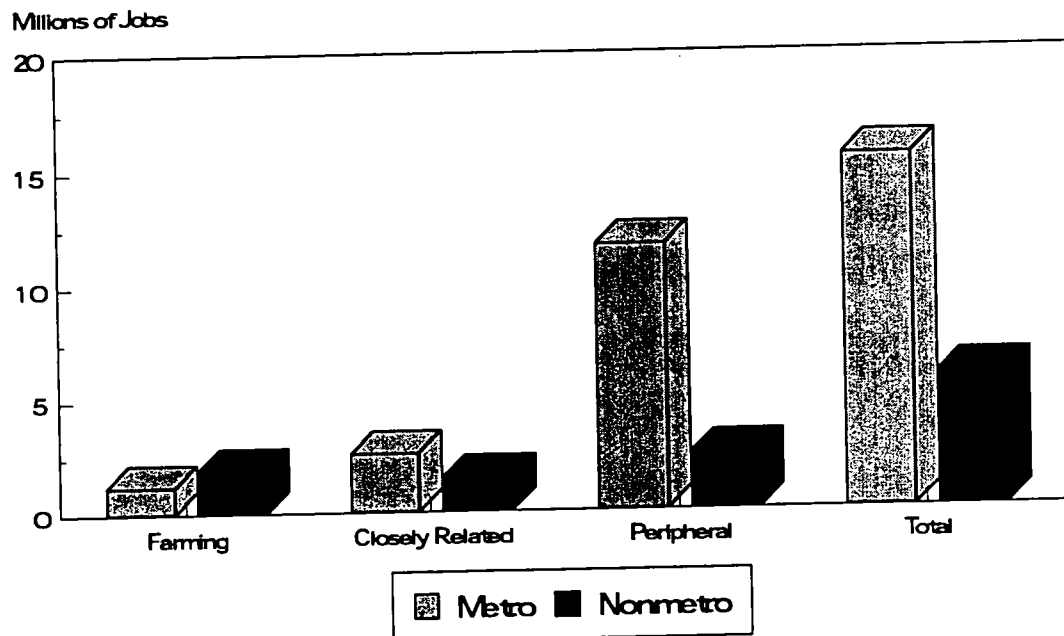
- Rural Economy at a Glance
- Farm Business Economics

at <http://www.econ.ag.gov/>

flow was in the opposite direction. Over 75 percent of nonmetro counties saw population growth in the 1990-95 period, up from 44 percent during the 1980s.

- Natural resources (land, timber, water) are performing a new role for many rural areas. Historically, natural resources have been important for their extractive value thereby providing jobs in farming, mining, and forestry products. But in the last two decades, the amenity value of natural resources has contributed to rural population and employment growth. For example, retirees are drawn to rural areas that are rich in scenic beauty and have a moderate climate thereby creating retirement-recreation based economies.

Most Farm-Related Jobs Are in Metropolitan Areas



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Farm Policy

U.S. AGRICULTURAL POLICY

U.S. farm policy has its roots in Depression era legislation of the 1930s when farm prices were depressed and farm income was significantly below income of the rest of the U.S. economy.

Over the decades, a series of legislative acts have revised the original farm programs to reflect the needs and

constraints of the times. The 1996 farm policy act, the Federal Agricultural and Improvement Act of 1996--changed the role of government in agriculture, continuing the evolution away from intervention in markets and embracing the use of direct payments to producers.

The 1996 Act is likely to increase economic efficiency and reduce the

may also bring increased income variability and increased responsibility for producers to manage price and market risk. Business strategies to reduce risk could have implications for farm sector structure and could accelerate the trend in use of production and marketing contracts and other forms of vertical coordination in agriculture.

History of U.S. Farm Policy

- The 1933 Agricultural Adjustment Act (AAA) was a landmark piece of legislation in the history of American farm policy--a major break from previous legislation. Prior to 1933, "farm" legislation had the intent to provide greater opportunities in the agriculture sector.

- The 1933 AAA was designed to address the "farm problem"--low prices (supply surpluses); instability and uncertainty in farm prices and incomes; and low incomes in farm and rural communities. The 1933 AAA gave the U.S. government a new role in the management of the farm sector.

- The AAA and subsequent legislation introduced commodity programs which included production and marketing controls and price and income support programs for many of the most important farm commodities.

- Conditions in U.S. agriculture and the broader economic and policy environment have changed dramatically since the 1930s, but until the 1996 Federal Agricultural Improvement and Reform Act (1996 Act), U.S. farm policy revolved around mechanisms that tied price and income supports to

production controls.

Conditions Have Changed...

- In the early years of farm programs, roughly one-quarter of the U.S. population lived on farms. The current share of population living on farms is less than 2 percent.

- Yesterday's farms were diversified, but today they are often highly specialized. The proportion of farms producing any one commodity covered by farm programs has declined over time as a result of increased specialization of production. For example, in 1949, 1 in 5 farms produced cotton, compared to 2 percent in 1992. In 1949, 59 percent of all farms produced corn for grain compared to 26 percent in 1992. In 1949, 55 percent of all farms produced dairy products compared to 7 percent in 1992.

- Farm commodity programs were developed when the average income of farm households was about one-half that of all U.S. households. With the possible exception of the World War II period, this low relative income status persisted well into the 1960s. Farm households generally achieved in-

come parity with all U.S. households during the 1970s. The situation has remained that way, except for the early 1980s.

- Improved access to rural non-farm jobs and off-farm income has played an important role in farm households achieving income parity. As discussed in the first section of this briefing book, farm households, on average, depend more on income from off-farm sources for family living than on income from farming.

...Bringing Pressures for Policy Reform

- The changing structure of the U.S. agricultural sector and increasing dependence on world markets built pressure for reform in U.S. farm policy.
- Farm program rules constrained the most efficient producers in that

their production decisions were tied to program parameters rather than to market prices. Additionally, program rules at times restricted the sector's ability to fully compete in the global market place. Acreage controls for some crops allowed competitors to expand.

- Government expenditures for agriculture rose to peak levels in the

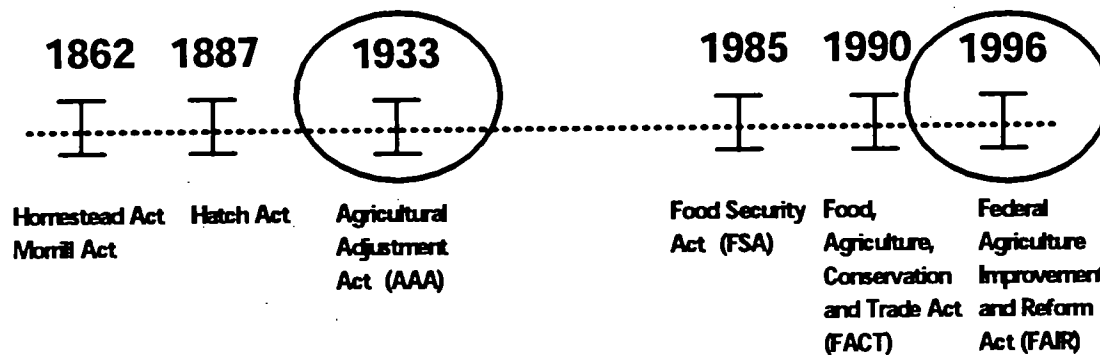
late 1980s, which increased the Federal budget deficit and induced non-agricultural interests to become concerned with farm program costs.

Commodity Programs Managed Downside Risk for Producers

- The U.S. farm sector's dependence on government programs and payments has varied over time. One measure of the ebb and flow of the sector's dependence on farm programs is the level of direct government payments to producers as a percent of gross cash income.

- Dependence on direct government payments is not, however, the only measure of Federal support for the farm sector. Incomes were also protected by a system of price supports that kept prices at or above a set floor price--the government acting as a residual market adjuster and accumulating stocks under weak market conditions. Also, annual supply management programs required the idling of land--more land being idled under weak market conditions.

U.S. Farm Policy

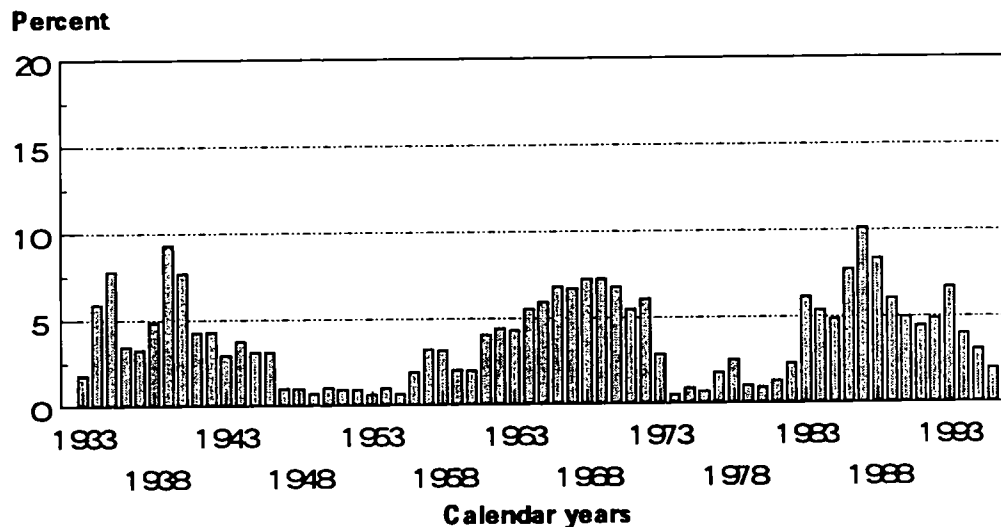


- Government payments over the 1933 to 1995 period ranged from 1 to 10 percent of gross cash income, as shown in the chart. The level, however, is not as important as the cyclical nature of the farm sector's dependence on government programs.

- Government payments were until 1996 linked countercyclically to market conditions. Under weak market conditions (low prices), government payments increased. Government payments tended to fall when market demand was strong and prices high. Essentially, the federal government through the commodity programs managed the down-side market/price risk for producers.

- It is important to keep this countercyclical nature of government programs in mind. It becomes important later in understanding the implications of the 1996 Act.

U.S. Government Payments, as a Proportion of Gross Cash Income, Appear to Cycle Through Time



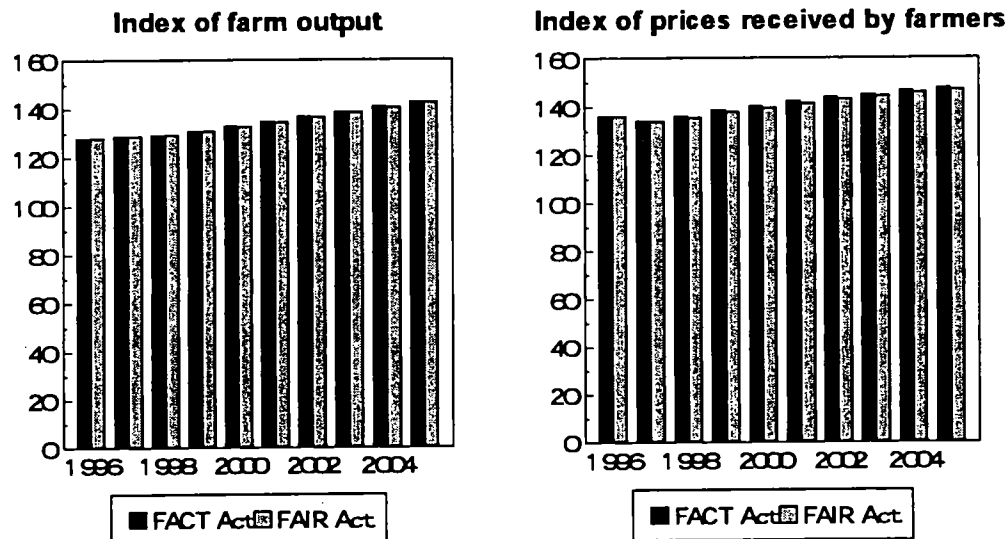
Represents direct government payments as a percent of total U.S. farm operator's gross cash income.
1996 is a forecast.

Regional Differences in Farm Program Dependence

- While direct government payments are 1 to 10 percent of gross cash income for the farm sector as a whole, they are more important in some regions than in others.

- In parts of the Southern Plains, the Western Corn Belt, and the Northern Plains, producers depend on government payments for 30 percent or more of their gross cash income. While many factors influence the dependence on government payments, the crop mix and the specialized nature of production, the size of the operation, and the degree of

Impact of Legislation on Output and Prices Is Minor



natural advantages (climate and soil productivity) are important determinants of dependency in these regions.

- The regional pattern of dependency on government payments, like the countercyclical pattern, is an important factor in understanding those areas likely to experience the greatest adjustment burden or pressure as a result of policy reform and the

implementation of the 1996 Act.

1996 Federal Agriculture Improvement and Reform (FAIR) Act

- The 1996 Act is another landmark in U.S. farm policy. First, it takes a major step toward phasing out com-

modity programs that have been in existence, in some form, since the 1930's. Secondly, it takes the United States to an almost fully market-oriented farm policy.

- In the market orientation sense, the 1996 Act is more evolutionary than revolutionary. It completes the process that began with the two previous farm acts (1985 and 1990) of cutting the link between farm production decisions and government policy signals sent through traditional commodity programs. The 1996 Act completes the move to market orientation by: decoupling planting decisions from program parameters; eliminating annual supply control programs; and, most importantly, it no longer ties government payments to market conditions.

- Responsiveness to market forces will generate economic efficiency gains and make the sector more competitive in the global marketplace. As income variability increases, producers will need to take more responsibility for managing market and price risk.

Impact of Legislation on Output and Prices is Minor

- Projections from USDA and the Congressional Budget Office (CBO) suggest that levels of supply, demand, and prices for most commodities under the 1996 Act will differ little from the levels projected under a continuation of the old (1990) farm act.

- There are two major reasons for this finding. First, operator decisions, at least at the margin, were already being driven by market forces, more so than program parameters, following the 1990 farm legislation. Second, the next ten years point to bullish commodity markets based on expected strong export demand that helps offset government withdrawal of price and income support mechanisms (see trade section of this briefing book).

Farm Income Higher with 1996 Act Contract Payments

- Under a continuation of the provisions of the 1990 Act, direct government payments (called deficiency payments, projected at \$11 billion over 7 years) would have been substantially lower than the contract payments called for under the 1996 Act (capped at slightly over \$36 billion

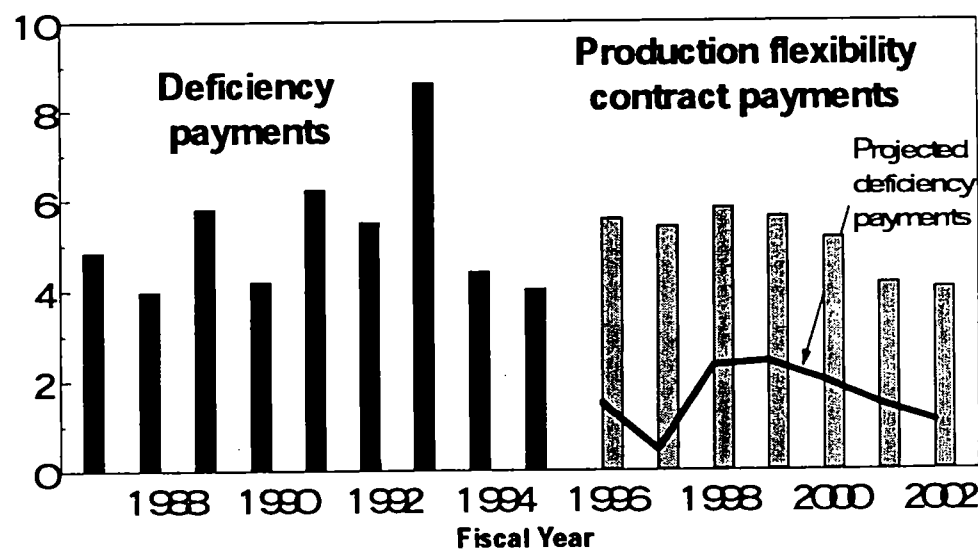
over 7 years). So farm incomes (cash income from the market plus government payments) will likely be higher under the terms of the 1996 Act than they would have been under continuation of the old law.

- Phasing out of commodity programs is not likely to lead to any large-scale displacement of farm

operators on a sector-wide basis. First, contract payments will add to farm income and can be used by producers to facilitate whatever financial restructuring and rationalization that needs to take place. Secondly, the farm sector, in the aggregate, is currently financially sound.

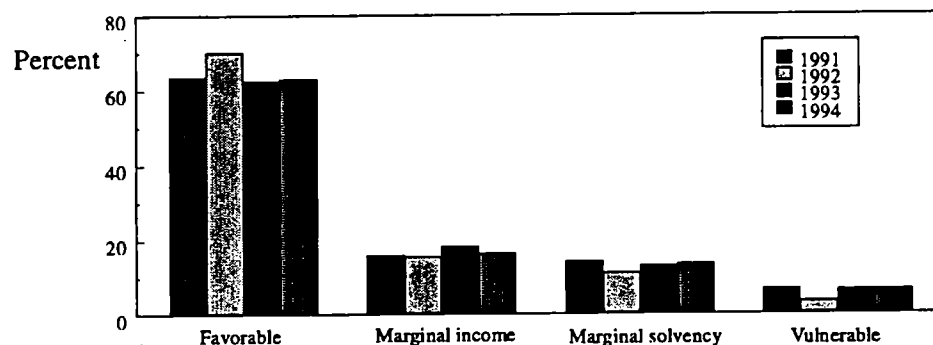
Production Flexibility Contract Payments

\$ Billion



Commercial Farm Financial Position

Most commercial farms that participate in government programs are not dependent on government payments (5 percent or less of gross farm income) and are in a strong financial position.



Even though payments do not represent a significant source of income, livestock farms are likely to be faced with transition issues given low incomes in 1994-95.

150,800 crop farms

Item	Dollars per farm
Gross farm income	\$230,237
Direct gov. payments	\$ 14,494
Net cash farm income	\$ 61,863
Net farm income	\$ 57,434

172,000 livestock farms

Item	Dollars per farm
Gross farm income	\$220,304
Direct gov. payments	\$ 8,360
Net cash farm income	\$ 37,659
Net farm income	\$ 24,375

Commercial Farm Financial Position

- Over 60 percent of commercial farms are in a favorable financial position and many of those farms are not dependent on government payments (payments account for 5 percent or less of gross farm income).

- Only 6 to 7 percent of commercial farms are classified in a vulnerable financial position, with a debt-to-asset ratio of 40 percent or greater. Consequently, little added displacement is expected to result from the 1996 Act.

Some Farms Under Pressure

- Reducing government influence on commodity production and marketing decisions means regions with natural comparative advantage--climate, soil productivity, alternative production possibilities, cost advantages, etc.--will be strengthened, but at the expense of "marginal" areas more dependent upon a "program advantage" than comparative advantage.

- Asset values, particularly land values, in marginal areas where values reflect existing commodity programs will drop. Areas with good productivity and cropping alternatives and less dependence on program returns could see asset values increase.

- Adjustment pressures will likely be greatest in the Northern Great Plains (wheat farms), the Western Corn Belt (mixed grain farms), and in the Southern Plains (wheat/cotton farms). There is a possibility of added stress in the Upper Midwest and the Northeast associated with reform in the dairy sector.

- The 34,000 farms identified as being most susceptible to financial restructuring have similar characteris-

tics: moderate size farms with average gross cash incomes around \$100,000; government payments averaging over 30 percent of gross cash income; and a more vulnerable financial position (13 to 25 percent of these farms have a debt-to-asset ratio exceeding 40 percent).

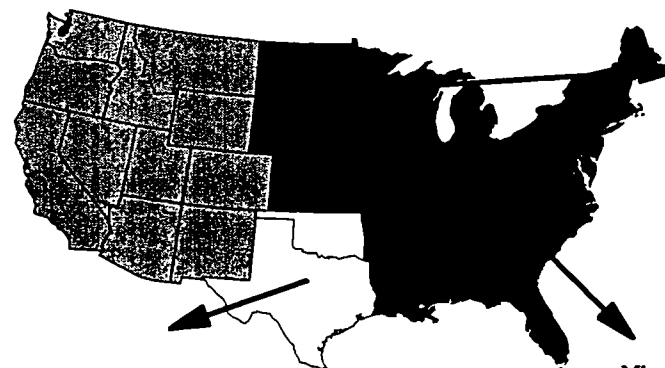
- Vulnerable regions could see an acceleration of farm consolidations and further concentration of production in a small number of large farms.

Market and Price Volatility Call for Risk Management Strategies

- Projected supply and demand conditions are based on "normal weather" and trend yield growth. In reality, we can expect to see continued commodity market volatility on the basis of year-to-year swings in domestic yields and export demand.
- Market and price volatility have been a hallmark of the agricultural sector. Under previous programs, the government played a large role in attempting to manage market/price risk in periods of weak demand--through various supply control and stockholding programs.

Farms Under Pressure

The financial transition will be greatest for 34,000 farms that are most dependent on government payments (20 percent or more of gross farm income).



Wheat farms

Moderate size farms with average gross cash income of \$90,000. Net farm income averaged \$15,000 during 1991-94. Off-farm income averaged \$21,908. Government payments averaged 34 percent of gross cash farm income. Thirteen percent have a debt/asset ratio of 40% or higher.

Crop sales the primary source of income with relatively small amount (8 percent) from livestock sales. On average, farmers own 800 acres of the 1,700 operated. Both cash and share rental arrangements have been used to expand operations. Fifty-six percent are age 55 year or older. Ninety-six percent consider farming their primary occupation.

Wheat/cotton farms

Moderate size farms with average gross cash income of \$110,000. Net farm income averaged \$25,000 during 1991-94. Off-farm income averaged \$32,200. Government payments averaged 36 percent of gross cash farm income. Twenty-five percent have a debt/asset ratio of 40% or higher.

Crop sales the primary source of income with relatively small amount (8 percent) from livestock sales. On average, farmers own 440 acres of the 1,600 operated. Both cash and share rental arrangements have been used to expand operations. Fifty-five percent are age 55 year or older. Eighty-eight percent consider farming their primary occupation.

Mixed grain farms

Moderate size farms with average gross cash income of \$103,000. Net farm income averaged \$4,500 during 1991-94. Off-farm income averaged \$23,076. Government payments averaged 30 percent of gross cash farm income. Sixteen percent have a debt/asset ratio of 40% or higher.

Crop sales the primary source of income with relatively small amount (9 percent) from livestock sales. On average, farmers own 200 acres of the 650 operated. Both cash and share rental arrangements have been used to expand operations. Twenty-four percent are age 55 year or older. Ninety-one percent consider farming their primary occupation.

- The 1996 legislation allows changes in market prices--not government programs--to "equilibrate" supply and demand. Will commodity prices be more volatile under the 1996 Act? Empirically, we don't know. But, cash farm income could be more volatile.
- U.S. producers are already using many market risk management strate-

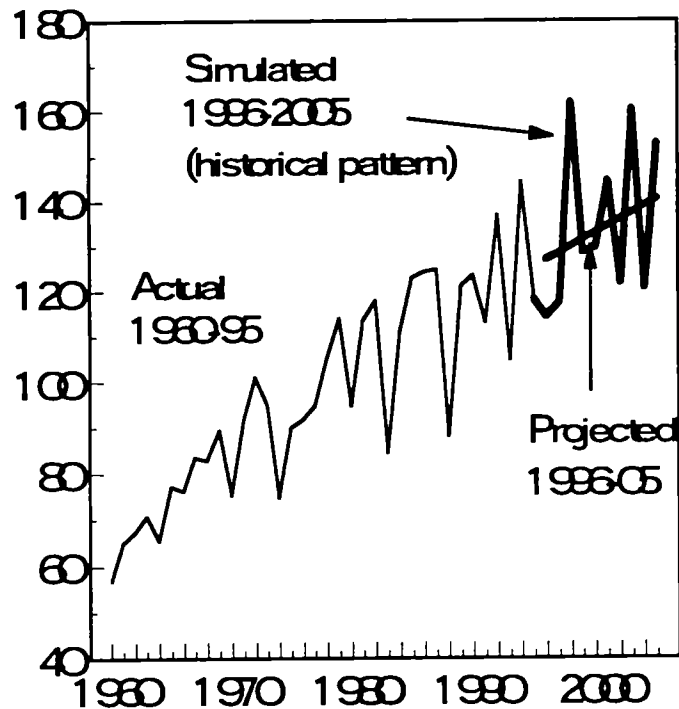
gies. Producers are more often using strategies such as keeping equity in cash and current assets, buying crop insurance, and spreading sales over the year than they are hedging in futures markets.

- How do size and ability to manage risk interact? Smaller enterprises with a greater dependence on off-

Corn Yields and Export Variability

Corn yields

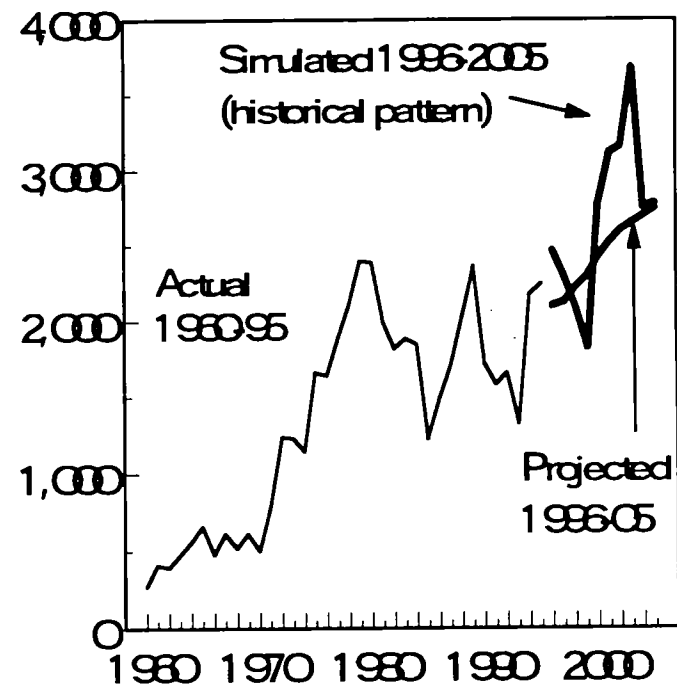
Bushels/acre



Baseline yield projections assume normal weather conditions throughout period.

Corn exports

Million bushels



Policy changes, political upheaval, or widespread crop failure could shift export demand in any given year.

farm income are in a stronger position to weather increased market volatility and income swings. Larger diversified operations are in a strong position to take advantage of production, marketing, and financial strategies to manage risk. Many of these larger farms, less dependent on government payments, are those already using a wide array of risk management strategies.

- The medium size farms (smaller commercial farms), appear to be the enterprises most in need of timely market information and a research and education program designed to identify alternative risk management strategies and to improve risk management skills. The 1996 Act essentially places a premium on management and the use of information to control costs and improve financial performance of farm operations

Risk Sharing via Production and Marketing Contracts is Increasing

- The issue of price and income volatility and managing market risk goes beyond the farm gate to the food marketing system.

• Agribusiness has strong interest in dependable supplies, stable prices and constant margins rather than more volatile prices. Agribusiness is likely to join producers in search for risk management options.

- In food industries not covered by previous farm programs, such as livestock and horticultural products, risk

Use of Risk Management Strategies, 1994

	Commercial farms				
	All farms	Program participants			
		All commercial farms	All participants	More than 10% gross cash income from payments	More than 20% gross cash income from payments
				Percent	
Hedge or use futures markets	11	26	35	34	29
Contract crop/livestock sales	20	48	57	55	57
Spread sales over year	39	67	75	76	68
Forward price inputs	16	42	53	58	57
Keep unused borrowing capacity/Open credit line	35	66	74	72	68
Keep equity in cash & current assets	54	80	84	81	75
Produce stable or low-variability income commodities	28	50	57	56	47
Government program participation	42	71	94	96	96
Purchase crop or livestock insurance	40	71	85	46	46

Source: 1994 Farm Costs and Returns Survey

Risk Sharing Via Contracts Is Low, But Increasing For Field Crops

Output under production and marketing contracts

Commodity	1970	1994
Field Crops		
Food grains	2	8
Feed grains	<1	13
Cotton	11	20
Livestock		
Broilers	92	92
Turkeys	60	66
Fluid grade milk	95	95
Hogs	1	13
Fed cattle	18	11
Specialty Crops		
Processed vgs.	85	88
Fresh vgs.	21	25
Potatoes	45	55
Citrus	84	88

sharing via production and marketing contracts has been a major risk management strategy.

- Output under production and marketing contracts for field crops is low, but increasing. The 1996 Act could accelerate that trend in use of production and marketing contracts and other forms of "vertical coordina-

tion" for field crops. Consequently, business strategies to reduce risk could have structural and vertical coordination implications.

Suggested readings on risk management in U.S. agriculture...

Harwood, Joy, Dick Heifner, Keith Coble, and Janet Perry. "Strategies for a New Risk Management Environment," *Agricultural Outlook*, USDA, Economic Research Service, October 1996.

...and suggested readings on U.S. agricultural policy reform:

Nelson, Frederick J., and Lyle P. Schertz, eds. *Provisions of the Federal Agriculture Improvement and Reform Act of 1996*, AIB-729, USDA, Economic Research Service, September 1996.

Young, C. Edwin, and Paul C. Westcott. *The 1996 U.S. Farm Act Increases Market Orientation*, AIB-726, USDA, Economic Research Service, August 1996.

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Andrew J. Mayock

01/07/98 11:59:39 AM

Record Type: Non-Record

To: Elena Kagan/OPD/EOP, Thomas L. Freedman/OPD/EOP, Cynthia A. Rice/OPD/EOP
cc: Barbara D. Woolley/WHO/EOP, Robert B. Johnson/WHO/EOP
Subject: DPC Follow-Up to Small Farmers Meeting

This e-mail tracks the outstanding issues from the President's meeting with small farmers for which your office is solely or jointly responsible. This Friday, January 9, a comprehensive memo will be sent to the President that updates him on these issues among others (see below for complete list). Our goal is to have responses out the door to each of the items.

By COB Thursday, please send me paragraphs (weekly report-style) which provide an update on each of these items.

Thank you.

Follow up Items for DPC Staff

DPC staff contact to work on farm policy here at the WH. Tom Freedman selected. (Is there something to add (e.g., Will he initiate a working group?))

Senator Robb's Tobacco Proposal. In conjunction with Legislative Affairs, Elena Kagan and Bruce Reed are drafting response to Senator Robb's proposal regarding tobacco.

Documents sent to President Clinton by Small Farmers. Additionally, Barbara Woolley is following up on the documents that were submitted to the President by the farmers with your office.

Request for a meeting on tobacco deal with the President and Federation of Southern Cooperatives/Land Assistance Fund (FSC/LAF) - Ralph Paige. Recommend Bruce Reed hold meeting with FSC/LAF. Woolley will follow up with Reed and then handle appropriate correspondence.

Request for a meeting on tobacco deal with the President by Commodity Growers Cooperative Association - Karen Armstrong-Cummings and Rod Kuegel. Recommend Bruce Reed hold meeting with FSC/LAF. Woolley will follow up with Reed and then handle appropriate correspondence.

Proposal for additional funding for welfare to work project by Hmong American Community - Toulou Thao. Recommend forward proposal to Cynthia Rice for appropriate follow up. Woolley will track and monitor.

*6000
500
C. A. Rice*
FWMS
SW

new projects

- done

BK

- C. A. Rice

BK

CF

K. J. Mayock

Farms
— 40

**Domestic Policy Council
Follow-Up on Small Farmers Meeting
January 8, 1998**

Working Group on Highlighting Issues in Farm Policy

The DPC is establishing a working group to research and promote issues of interest to farmers. The group will emphasize finding issues of importance to rural communities that deserve attention as part of the Administration's public agenda. Tom Freedman of DPC will coordinate the working group, which will include representatives from USDA, NEC, CEA, Treasury and OPL.

Meetings With Tobacco Farmers

Bruce Reed will hold meetings with interested tobacco farm representatives to explain Administration positions on tobacco and coordinate with the needs of farmers. He will meet with farmer representatives including Ralph Paige.

Carl Whillock continues to serve as the primary Administration contact at the DPC for on-going agricultural issues.



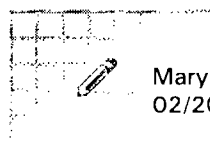
Thomas A. Kalil

02/20/98 05:40:55 PM

Record Type: Record

To: Mary L. Smith/OPD/EOP
cc: Thomas L. Freedman/OPD/EOP
bcc:
Subject: Re: Distance Learning for Rural Areas

Mary L. Smith



Mary L. Smith

02/20/98 10:47:01 AM

Record Type: Record

To: Thomas A. Kalil/OPD/EOP
cc: Thomas L. Freedman/OPD/EOP
Subject: Distance Learning for Rural Areas

Tom and I have been asked to come up with a list of rural/farmer issues. Is there anything going on with distance learning, particularly in rural communities? Do you know of any other rural initiatives that you think we should be pushing? Thanks, Mary

#1. Learning Anytime, Anywhere -- not just rural -- but will be especially helpful to rural

#2. Distance Learning and Telemedicine program
<http://www.usda.gov/rus/dlt/dlml.htm>

#3. FCC program to provide discounts to rural health care facilities

<http://www.fcc.gov/healthnet/>

Not yet up and running

#4. New idea -- digital library for Rural America. Imagine that farmers and other rural Americans could easily search:

all of the research funded at our land grant colleges

Farms

*Call
Glen F.*

*Edwards
Farm
Agrib*

"lessons learned" from rural development
programs in housing, tourism

etc., etc.

I did a write-up for this for the Rural Fund for America,
and got some language on telecom in the solicitation,
but didn't do a whole lot of follow-up with USDA.

Let me know if you are interested.



DEPARTMENT OF AGRICULTURE
OFFICE OF CONGRESSIONAL RELATIONS
WASHINGTON, D.C. 20250-0100

Farmers

FAX COVER SHEET

DATE: 7-7-97

COVER SHEET PLUS 2 PAGES

TO: Tom Freedman

FAX # 456 - 7431

PHONE # _____

FROM: Dave Carlin

USDA - OFFICE OF CONGRESSIONAL RELATIONS
ADMINISTRATION BUILDING - ROOM 213A
JEFFERSON DRIVE, S.W.
WASHINGTON, D.C. 20250
(202) 720-7095

REMARKS: _____

KY. Tobacco Farmers, Bjt, 0718 (102)
Farm leaders work for relief proposals

LOUISVILLE, Ky. (AP) There are signs that farmers will come out of the legislative process in better shape than they did under last month's \$368.5 billion tobacco settlement.

Kentucky and North Carolina farm leaders are working on a package of relief proposals. Also, a key tobacco industry negotiator appears supportive of the farmers, and health advocates say they want to protect the growers from sudden economic upheaval.

"I feel very strongly that farmers should not be left out of the deal," David Kessler, former commissioner of the U.S. Food and Drug Administration, said recently. "I think that's a very high priority."

These groups don't necessarily agree, however, on the form aid for farmers should take. The options include compensation for lost income, limits on the amount of foreign-grown tobacco in American cigarettes and a buyout program to encourage farmers to stop growing tobacco.

Economic projections show the cutback in smoking that results from the agreement could translate into more than a 50 million-pound reduction in the use of burley leaf, most of which is grown in Kentucky.

With a selling price close to \$2 a pound, that's a lot of lost money.

But the only thing the deal does for farmers is guarantee that the FDA's enhanced regulatory authority won't extend to tobacco cultivation.

The settlement, however, is far from settled. The agreement must be drafted into legislation, passed by Congress and signed by President Clinton.

A lead industry negotiator, North Carolina lawyer J. Phil Carlton, says he wants to help the farmers.

Carlton, the son of a tobacco farmer and until recently the owner of a tobacco farm, told The Courier-Journal last week that the farmer issue will definitely be on the table as negotiators draft the legislation to submit to Congress.

"We're willing to talk about that," Carlton said of one possibility the growers are interested in: a guarantee that cigarette makers will commit to use a certain amount of domestic tobacco.

The industry, according to Carlton, also is willing to consider paying for tobacco crop insurance and the tobacco price-support program's administrative costs should Congress cut off the funding, as some have proposed.

And public health officials want to see the farmers get help, although their main objective is not compensation.

Instead, the health groups want to use money to entice the farmers out of the tobacco business and out of their longstanding political alliance with the cigarette companies.

Their idea is either to pay farmers to retire their growing quotas or give them money to try alternative crops.

Last month, health group negotiators proposed that the settlement set aside about \$150 million a year mainly for that purpose. But Carlton said he rejected that idea, and it was not included in the settlement. He said the proposal was not comprehensive enough.

One of four interagency panels President Clinton set up to review the agreement will focus on the tobacco industry, including the economic impact on the growers.

Unlike the cigarette makers, the farmers come to the legislative process seemingly unblemished by the controversy and distrust that for decades gripped the smoking issue.

"They've not been willing conspirators. They've been pawns," Indiana Attorney General Jeff Modisett said.

Sen. Wendell Ford of Kentucky has said repeatedly that without protection for the farmers, he won't support implementation of the bill.

Ronny Pryor, chief lobbyist for the Kentucky Farm Bureau, wants farmers compensated for lost sales and quota reductions, and he insists there would be little interest among burley growers in a quota buyout. Tobacco is too lucrative to give up, he said.

But Pryor indicated there is nevertheless room to please both farmers and the anti-smoking side. He suggested the possibility of a compromise that would compensate farmers while also helping them move into alternative crops. "We don't see it as an either-or thing," he said.

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Received by NewsEDGE/LAN: 7/4/97 5:45 AM