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The 2014 Farm Bill, Commodity Subsidies, and California Agriculture

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The Agricultural Act of 2014 replaced some outmoded programs with new subsidies. It reauthorizes hundreds of initiatives and programs, from nutrition assistance to export subsidies. The nutrition programs continue to use most of the budget, while farm subsidies that focus on risk management gain new support.

Also in this issue

In many ways the Agricultural Act of 2014, signed by the President on February 7, represents a "business as usual" farm bill. Weighing in at about 360 pages of dense text, it updates a myriad of government subsidies such as those for nutrition assistance, farm commodity programs, farm environmental investments, rural internet service, international commodity promotion, and research and development. Despite its scope and complexity, many food and agricultural programs, including school lunch programs, milk marketing orders, most crop insurance provisions, and most environmental regulations continue to remain mostly outside the farm bill.

The Supplemental Nutrition Assistance Program (SNAP), which was modified only slightly, again dominates the budget. SNAP accounts for almost $76 billion per year of projected spending, out of about $960 billion of the farm bill budget for the next ten years. The rural and agricultural programs account for about $20 billion per year in projected outlays. Overall, the agricultural titles replace some outmoded commodity subsidies with new versions, consolidate some environmental subsidies, and renew or update hundreds of individual programs.

Although many provisions of the 2008 farm bill were scheduled to expire in September 2012, contentious debate over SNAP, dairy policy, and farm subsidies delayed passage of the new farm bill for about 18 months. Some programs were continued on a temporary basis and some simply lapsed in the interim. In the end, many of the most contentious proposals were left aside and a consensus developed to move forward with less change than many proponents had advocated. For example, efforts to significantly reduce SNAP outlays by tightening rules were not included. Likewise, a program to manage dairy supplies in times of low prices was not included in the final bill.

This article will not attempt to summarize hundreds of individual programs; rather, we will characterize the likely economic implications of modifications to the farm commodity subsidies under the new farm bill that seem most relevant to California. We begin with dairy program changes because the dairy industry is the largest farm commodity industry in California by revenue, and is tied closely to the hay and forage industries and the cattle feed industry.

Dairy Programs

Balagtas, Sumner and Yu (2013) previewed the state of the farm bill dairy deliberations. As expected, the Agricultural Act of 2014 did eliminate the long-standing price support and export subsidy programs that had slipped to irrelevance. It also avoided the complex farm-by-farm federal supply management that had been supported by the National Milk Producer Federation, but had mixed support among producers more broadly. Processing firms, other than farm cooperatives, generally opposed federal supply management, pointing out that it would disrupt market signals and milk

Table 1. Commodity Program Payment Triggers for Crops Important to Some California Farms: Comparing New Reference Prices to the Old Target Prices

	2014 Farm Bill Reference Price	2008 Law Farm Bill Target Price
Corn	$2.63/bushel	$3.70 per bushel
Wheat	$4.17/bushel	$5.50/bushel
Medium grain rice	$10.50/ cwt	$14.00/cwt

availability just as the United States had become competitive in export markets.

As expected, the 2014 Act also leaves aside changes to Federal Milk Marketing Orders, which regulate prices that private buyers must pay for farm milk and how revenues from such sales are allocated among farms. That means the complex of federal regulations for milk pricing, which apply regionally, remains unchanged from what was implemented 15 years ago.

California has operated outside the federal order system for about 80 years, but there is much current attention to the potential for California to shift from state to federal dairy pricing regulation. The Agricultural Act of 2014 offers California the option to join the federal system on a state-wide basis, if producers vote to do so. The Act also reaffirms that a federal order that encompassed California could use a milk quota system to allocate some of the pooled milk revenues back to producers–a procedure that California has used for about 45 years to distribute what is now about 4% of milk revenues under the California order. The Act gives no specifics about how the California system would be incorporated into a newly created federal order, which generally involves a long and complex process.

The main new federal dairy program, the Milk Margin Protection program, offers payments to make up for low margins between milk revenue and feed costs. More specifically, after the program is implemented on or before September 1, 2014, enrolled dairy farms would receive payments based on the difference between the monthly national average "all milk" price per hundredweight and an index of national corn, soybean, and alfalfa hay prices converted to represent the typical feed cost per hundredweight of milk.

The legislation sets premiums that start at zero for coverage at the lowest margin ($4 per hundredweight) and rise as the coverage trigger rises up to $8 per hundredweight. Premiums are higher for a production history of more than 4 million pounds of milk per year (production of about 170 cows at the California average production per cow). Given the size distribution of dairy farms in California, the higher premium schedule will apply to almost all milk production here.

Milk prices have risen while corn and soybean prices have fallen dramatically since the legislation and the basic premium schedule was developed in 2012. That means the probability of margins falling below any specified margin has declined and the expected value of payments for any given coverage level has also fallen. Thus, while still positive, the expected net payoff to margin protection may be relatively low for most California producers and the incentive to pay for the higher coverage levels is lower than it may have seemed just a year or two ago.

Subsidies for Traditional Program Crops

Program crops (primarily feed grains, wheat, rice, oilseeds, and cotton) have received the bulk of farm bill support over the years and the Agricultural Act of 2014 is no exception. However, as has occurred with several recent farm bills, the form of payments to these farms has changed in response to political trends and market conditions.

Government payments triggered by low commodity prices dried up after the jump in farm prices in 2008 and 2009. Since then, program crop subsidies have consisted primarily of $5 billion per year in direct payments that are based solely on each farm's production history of specific program crops—not on current production or prices. Direct payments, originating with the 1996 farm bill, were designed specifically to reduce the link between subsidies and incentives to produce program crops, with the aim of reducing distortions in crop planting and commodity markets. The Agricultural Act of 2014 reverses this approach, by replacing direct payments with new subsidy programs that reconnect subsidies to specific production, prices, or revenues of specific crops.

Under the 2014 Act, eligible farms that produce "covered" crops, mainly grains and oilseeds, will choose between payments triggered by commodity prices, county-wide revenue, or individual farm revenue. Farms have the option of price-based payments (Price Loss Coverage) or one of two forms of revenue-based payments (Agricultural Risk Coverage). The "Price Loss Coverage" pays producers of covered crops whenever the market price falls below the reference prices written into the law.

Besides payments being tied to production of specific crops, the new law raises "references prices" that are used to trigger payments from their counterparts in the 2008 farm bill. It also allows farmers the option to use a revenue trigger for payments if the new reference prices do not seem attractive

In California, with limited production of feed grain, wheat and oilseeds, rice farms have the greatest potential payments from these programs. The Act raises the reference prices that trigger payments. For example, the reference price for rice is now $14 per hundredweight—up from $10.50 per hundredweight under the 2008 Act (Table 1). The new farm bill raised the expected values of price-triggered payments for all the covered commodities. Nonetheless, given high projected market prices for medium-grain rice, the expected payments for rice are probably lower than the payments under the previous law.

Alternative subsidies under the Agricultural Act of 2014 can take the form of revenue guarantees under the Agricultural Risk Coverage (ARC) program. For farms with a base acreage of covered crops, the county-wide revenue version of the program pays when the county's average revenue for that crop falls below 86% of a five-year moving average of past revenue (adjusted for lots of complications). Thus, the county-based ARC pays off crop-by-crop.

Alternatively, a farm may enroll in an ARC program that pays when the revenue of the whole farm falls below 86% of that farm's average revenue (again, subject to many complicated provisions). This farm-specific trigger does not apply crop-by-crop and therefore more diversified farms, which have less-variable farm revenue, would be more likely to choose the county-based program. Conversely, more specialized farms with more variable revenues would be more likely to choose the farm-based program. In California, rice farms tend to be specialized and, while rice yields do not vary much from year-to-year, prices may move enough to trigger payments—especially given very high medium-grain rice prices within the past five years.

Crop Insurance

Most features of the federal crop insurance program, which is permanently authorized under the Federal Crop Insurance Act and not in the farm bill, do not change under the Agricultural Act of 2014. The subsidies include administration and operations costs, reinsurance provided to insurance companies, and about 60% of the premiums charged to growers. As summarized by Lee and Sumner (2103), crop insurance programs now cover many fruit and nut crops, some vegetables, as well as most field crops—except hay. For the field crops, most participants choose revenue insurance while for many tree, vine and vegetable crops, only yield insurance is available.

Even though most features do not change, the Congressional Budget Office (CBO) scored Title XI, the crop insurance title, as adding about $5.7 billion to the likely costs of the 2014 Act over the next decade. About 90% of this new spending derives from two new programs authorized in the new law.

First, a new area-wide program for program crops, the Supplemental Coverage Option (SCO), provides additional coverage on the portion of revenue shortfalls that would fall under the deductable amounts under most individual crop insurance policies. The SCO, with 65% premium subsidies, adds about $1.7 billion over 10 years. The SCO is unlikely to be of much use to California producers.

The new Stacked Income Protection for cotton (STAX), which operates similarly to SCO, but with 80% premium subsidies, replaces the previous upland cotton programs. The STAX program adds about $3.3 billion to CBO-projected outlays over the nine years after it begins operation in 2015. Upland cotton used to be a significant crop in California, but USDA surveys indicate farmers plan to plant only 60,000 acres in 2014.

As a part of its effort to expand crop insurance coverage, the 2014 Act directs USDA to develop more attractive crop insurance programs for organic crops, including basing insurance offerings on organic crop prices. Currently, crop insurance indemnities for organic crops often use prices of conventional counterparts because it has been difficult to establish organic market price benchmarks. USDA must offer the new policies by 2015. Using the lower conventional crop prices reduces the cost of insurance to growers and the USDA, but reduces the benefits to growers and may inhibit participation. The CBO projects outlays for the initiative at less than $1 million per year, so they do not expect widespread new participation.

Other Features of Interest to California Agriculture

The Agricultural Act of 2014 includes a Horticulture title that builds on programs included in the 2008 farm bill. The Research, Nutrition and Trade titles also include provisions of interest to horticultural industries. Continuation of the specialty crop block grant programs funds projects in marketing, research, food safety, and other purposes. Funding ranges from $72.5 million to $85 million per year, which is somewhat higher than the 2008 farm bill authorized. Targeted horticultural research authorized in the Research title is even larger and attempts to redress what had been perceived as a lack of appropriate support for horticultural commodities.

The 2014 Act continues two long-standing international marketing programs, the Market Promotion Program and the Foreign Market Development Program. Funding is authorized at $234.5 million per year and a significant share of the funds are available to California export commodities such as wine, almonds, and many more. These funds are crucial to the operations of several California organizations that undertake global marketing efforts.

Organic agriculture receives particular attention. The Act sets $100 million of mandatory research funds dedicated towards projects tailored specifically to organic agriculture. The Act allocates an additional $30 million over a decade in subsidies for organic certification. Of course, since organic certification is now more common in California, this subsidy may increase competition for California organic producers. Other provisions support farmers markets, additional market news and data, produce safety education, and more.

Provisions Not Included in the 2014 Act

Of course many proposals never make it into legislation and most of those proposals interest only a few advocates. For this farm bill cycle, two issues garnered an usual amount of national attention.

California's Proposition 2 and subsequent legislation are scheduled to regulate the housing for egg-laying hens beginning in 2015. The egg industry urged a farm bill provision that would set national standards for hen housing that would have superseded the California rules. Most of the egg industry, which generally opposed California standards, urged that a uniform national standard was preferable to state-by-state standards. That provision was also supported by certain animal welfare advocates, but failed to gain sufficient support to be included in the final negotiations.

The other egg-related provision would have blocked application of California standards for hen housing on eggs produced in other states and shipped into California. That amendment also failed to gain sufficient support, so the 2014 Act left the status quo in place under which, unless blocked by legal changes in federal court, California will apply hen housing standards for shell eggs consumed in California—no matter where they are produced.

Another livestock-related provision dealt with labeling certain retail meat cuts based on the country of origin of the livestock from which the meat is derived. The proposed amendments, supported by the major meat processing, hog and cattle organizations, would have rolled back somewhat current regulations that have implemented provisions of the 2008 farm bill. The proposals failed to find sufficient support in the conference committee writing the final bill and so the regulations implemented in November 2013 remain in force. This issue remains controversial. On April 3, 2014, Frank Lucas, the Chairman of the House Agricultural Committee stated, "It is hard to think of a greater disappointment than our inability to address the economic dislocations that have already occurred, as well as those yet to come, associated with our flawed mandatory county-of-origin law."

Final Remarks

As usual, the Agricultural Act of 2014 contains hundreds of programs and provisions that will distribute billions of dollars in small amounts to millions of individuals and groups. SNAP recipients dominate the numbers of direct beneficiaries and the total outlays. Within agriculture, hundreds of thousands of groups and individuals, ranging from local farmers' markets to large oilseed producers and wildlife preserves, all have programs that distribute funds tailored for their use. In the end, this collection of beneficiaries finally overcame policy objections and fiscal restraint to add the latest in the string of farm bills that go back more than 80 years.

Given the distribution of crops grown in the state, California continues to be a small beneficiary of farm commodity subsidies relative to its share of the value of agricultural production. The importance of payments from commodity subsidies declines further as California shifts even more land and water away from field crops such as cotton.

Two trends represented in the 2014 Act offset the reduction in commodity subsidies. First, crop insurance subsidies have become more important for fruit and vegetable crops and Congress has signaled that this trend will continue. Second, the expanding collection of programs, each with relatively small budgets, focus benefits on specialty crops, organics, locally marketed produce, and related topics of interest in California.

The Agricultural Act of 2014 is a collection of policies and programs, with many disparate beneficiaries and no over arching theme. The Act garners much less attention within California agriculture than it does in other important agricultural regions in the United States for the simple fact that the share of revenue from government subsidies is much less here than in those other regions. Nonetheless, California farms that grow the supported commodities do receive substantial support, and the Act contains so many other provisions that there is likely to be something for everyone, somewhere in its 1000 pages.

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For additional information, the authors recommend:

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