American Farmland Trust

Heartland Research Group

Proceedings of the Workshop
February 25, 2005
St. Louis, Missouri

Summary of the Heartland Research Group Workshop

Flipcharts: Group Discussion Outputs

Small-Group Discussion Outputs on Goals for Farm Policy and Payments

Notes from Table Discussions

SUMMARY OF THE FIRST MEETING OF THE HEARTLAND RESEARCH GROUP
Reforming American Farm Policy
March 3, 2005

On February 25, 2005, twenty-three producers, a land manager and two policy experts from America's heartland met with American Farmland Trust (AFT) staff to discuss reform of current farm policy. AFT sought out participants who understood farm programs, anticipated change and welcomed the opportunity to be sounding boards for research and policy development. The Heartland group covers the states—IA, IN, KY, MN, MO, OH and SD. The assembled group closely fit the profile of U.S. farmers in how they use government payments and how this influences their farming decisions. The Heartland Research Group is one of three research advisory groups providing their perspectives as AFT drafts a reform framework for the 2007 Farm Bill.

The group believed that reform is coming, driven partly by a tightening federal budget and the need to comply with World Trade Organization rules. Some feared the change but others saw reform as an opportunity to improve U.S. agricultural competitiveness. Skepticism tempered the feeling of inevitability since often a real crisis is needed for reform to happen. Participants identified the desired goals for a new farm policy although we did not try to reach consensus. Ideas included:

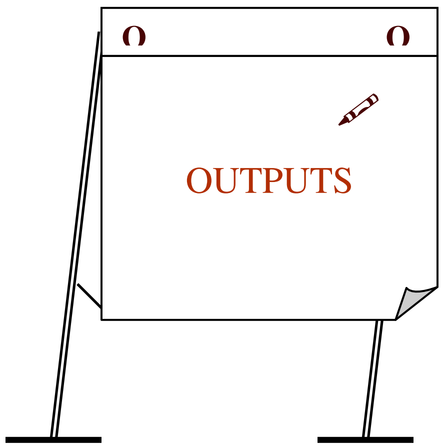
- Enhancing our competitiveness in world markets;
- Improving the nation's diet;
- Conserving natural resources;
- Increasing rural development opportunities;
- Providing opportunities to improve the economic viability of farm operations;
- Improving global and domestic food and energy security; and
- Empowering farmers.

During the facilitated sessions, agriculture leaders and producers discussed what's good and bad with current farm policy. The group identified over fifty "good" and "bad" points and voted on the most important. They wanted to keep the good aspects of existing policy while changing the bad elements. The farmers wanted to keep elements in current farm policy that allow planting and production flexibility, provide incentives for conservation, are market-oriented, put conservation dollars on working lands, provide incentives for energy production, reward good actors for conservation (like the Conservation Security Program) and provide a safety net (good risk protection and stability for producers/income). They also wanted to change elements that inhibit innovation, distort land use, encourage payments to be capitalized into land values, do not provide adequate incentives for the production of environmental benefits and encourage pass through of dollars to other asset owners.

Four small groups then independently designed their ideal farm policies:

- One of two options: permanently buy-out base acres and replace those subsidies with new production support programs that address national priorities (energy, environment, food security, rural development, permanent farmland protection) coupled with access to some crop and disaster insurance. Or create a better safety net offering income protection, risk insurance, farmer savings accounts and disaster crop insurance.
- Shift government payments to produce environmental benefits coupled with a comprehensive approach to risk management and investments in public research for public benefit.
- Transition to outcome-based conservation programs, establish an actuarially-sound, revenue-based insurance system, keep direct payments as a bargaining chip to use with other countries to gain market access until no longer needed and increase funds for research, economic incentives for rural development and energy production.
- Design a solid safety net to address risk that encompasses disaster relief, fold conservation programs into a renamed Conservation Security Program containing a robust bio-energy component and provide dedicated funds for technical assistance, value-added innovation and publicly funded research.

Over the next six weeks, AFT will engage two additional research advisory groups of producers in the Northeast and Great Lakes states (the Northern Crescent) and in the coastal states where most fruits and vegetables are grown (the Fruitful Rim). AFT also will organize meetings/forums with a wide range of producers over the next four months including western ranchers, limited-resource farmers and producers in California and the Mid-Atlantic states. Based on this feedback, AFT will design a farm policy reform framework and analyze possible impacts over the summer. The three research advisory groups will reconvene in the fall to react to this work and help improve the design.


OUTPUTS

o Group Discussion Outputs o

I. Drivers of Change

- Globalization of agriculture
- Need to comply with WTO rules
- Technology: biotechnology, digital technology, other rapid technological advances
- Consumer empowerment
- Accountability to taxpayers in a transparent policy environment
- Federal budget tightness
- Income gap in rural America
- Energy awareness
- Advocacy for rural development, conservation, energy interests
- Questions about sustainability of U.S. agricultural competitiveness
    - → Excess capacity
    - → Rising land values

Group Discussion Outputs

II. Reactions to the Idea of Major Farm Policy Reform

- Inevitability: “Change is coming”
- Skepticism
- “Scared”
- Need a crisis for reform to happen?
- Seen as an opportunity
- “Pie-splitting” will occur
- Security needed
- Political palatability a factor
- Moderation in reform
- Urban/suburban image/understanding of agriculture important
- Transition with minimal disruption desirable
- “Getting off the bubble”

o Group Discussion Outputs o

III. Desired Objectives of Farm Policy

Group-think about rationale for current/future farm programs. No consensus reached and no prioritization attempted

- Enhance international competitiveness of U.S. agriculture
- Improve nation's diet
- Achievement of a consumer-driven, global agriculture
- Conserve natural resources
- Enhance agri-environmental quality
- Increase rural development opportunities
- Survival of independent farm operations
- Provide opportunity for economic viability of farm operations
- Global food security: affordable and available food, worldwide
- Domestic food security
- Food safety
- Energy security
- Empowerment of farmers

o Group Discussion Outputs o

IV. What's Good with Current Farm Policy

(number of votes)

1. Voluntary incentives for conservation (13)
2. Market oriented (13)
3. Have a choice on conservation
4. Payments are guaranteed (2)
5. Offers stability for producers (5)
6. Fragile land is taken out of production (6)
7. Rewards good actors for conservation (CSP) (11)
8. Lots of money in the farm sector (3)
9. Direct and counter-cyclical payments are simple for farmers (check comes in the mail)
10. Has increased the wealth of agricultural land owners (subset of #8)
11. Good risk protection (10)
12. Stabilizes farm income (4)
13. Encourages conservation
14. Puts conservation dollars on working lands (13)
15. No large grain reserves
16. No supply management
17. WTO sensitive (8)
18. Counter-cyclical payments are sensitive to markets (4)
19. Increase in wildlife
20. Broad acceptability of conservation goals
21. CRP filter strips provide benefits to farmers and the public
22. Has maintained a strong agricultural economy and consistent food supply (2)
23. Value-added producer grants (2)
24. Market pull for bio-based products
25. Livestock and crop insurance
26. Environmental Quality Incentives Program (EQIP)
27. Planting flexibility (18)
28. Easy for USDA to administer
29. Opportunity to bring more land into production
30. Banker friendly

o Group Discussion Outputs o

What's Good with Current Farm Policy (continued)

31. Increased wealth for rural companies
32. Keeps corn, bean, cotton, livestock increasing by decreasing potential competition from fruits and vegetable producers
33. Beginning to decouple payments (includes deficiency, countercyclical and Conservation Security Program payments)
34. Does not infringe on property rights (1)
35. Maintains leadership by U.S. in technology development
36. Forced the European Union to come to the negotiating table and end export subsidies
37. Lots of dollars to work with (1 percent of the federal budget)
38. Energy title (12)
39. Dollars for good conservation to improve the infrastructure protecting land
40. Ability to identify acres for homeland security (1)
41. Can opt in or out of programs from year to year
42. Has kept producers on the farm
43. Economic signaling is still effective (1)
44. Beginning farmers programs (1)
45. Nutrition program helps bring in more supporters and more food security
46. Rural infrastructure support
47. Assures bountiful supply of commodities
48. Reliable sources at a steady rate
49. Allows for excess stock to be held privately (1)
50. U.S. prices go to world prices (7)
51. Research is supported
52. Good operators have flexibility and opportunity to enhance income (7)
53. No means test on income
54. Doesn't inhibit or interfere with disaster relief
55. Forces WTO's hand on market access (1)
56. Has influenced interest in green payments globally

o Group Discussion Outputs o

V. What's Wrong with Current Farm Policy

(Number of votes)

1. Lots of money in farm sector (good and wrong)
2. Increased the wealth of rural landowners and companies (good and wrong)
3. Too many deer
4. Keeps producers on the farm (good and wrong) (2)
5. Payments inhibit innovation (15)
6. Interferes with markets (crop insurance and LDPs) (1)
7. Not enough flexibility (crop to pasture) (1)
8. No actuarial basis for crop insurance (1)
9. Program is not simple with high transaction costs to track land use (1)
10. EQIP is inconsistent and complex (2)
11. Has expanded the corn belt (2)
12. Programs create a lack of trust between urban and rural residents
13. Programs create a lack of trust between farmers
14. Some payments are unnecessary
15. Pass-through of federal dollars to other asset owners (9)
16. Crop insurance costs too much (3)
17. Payments do not hit target group
18. Allows inefficient producers to survive (2)
19. Inhibits structural adjustments to global competitiveness (10)
20. Excludes many types of producers
21. Encourages overproduction by creating artificial markets (1)
22. Payments are capitalized into land values (12)
23. Inadequate incentives for production of environmental benefits (10)
24. Agriculture looks like it's greedy (1)
25. Farm programs are too reactive (2)
26. Payments are based only on production (5)
27. Encourages high cash rentals and consolidation
28. Crop insurance encourages production on unsuitable lands (3)
29. Public perception that some farmers are getting big dollars (bad image) (3)
30. Inconsistent administration of programs from place to place and program to program (3)

What's Wrong with Current Farm Policy (continued)

31. Disaster payments are pork and discourage crop insurance
32. Failure to support production of livestock (too many regulations) (4)
33. Subsidies create "ill will"
34. Livestock price insurance program is less competitive than current tools
35. Creates dependency
36. Rube Goldberg construction inhibits markets
37. De-emphasizes public funding for research (5)
38. Lack of flexibility for grazing on conservation lands (1)
39. No guarantees to global market access
40. Agriculture is held to a different standard compared to subsidies for other industries
41. Distorts land use (13)
42. Causes a lack of technology adoption (2)
43. Inhibits entry/exit of labor and capitol into agriculture (1)
44. Good programs are under-funded (2)
45. Inhibits entry by young farmers
46. Direct payments do not provide any value to the public (3)
47. CRP competes with young farmers and distorts land markets
48. Farmer preference would be to make all dollars from the market
49. Wedge between farm operators and land ownership
50. No strategic grain reserve
51. Inadequate technical support delivery system (2)
52. Programs often robbed to fund another
53. Programs do not help mid-sized farmers
54. Divisiveness between farm groups over payment limits (1)
55. Conservation programs don't offer biggest bang for the buck (1)
56. Conservation programs too narrowly focused (inadequately targeted) (2)
57. Conservation programs don't work well together (1)
58. Programs don't force producers to understand economic drivers (6)
59. Farm bill doesn't promote production of food and fiber as a national security interest (2)
60. Internal turf battles (NRCS and FSA)

o Group Discussion Outputs o

What's Wrong with Current Farm Policy (continued)

61. Does not support rural communities (2)
62. Imbalance between flexibility and uniformity
63. Allows NRCS to use "flawed" technology (2)
64. Not enough dollars
65. Doesn't take away the right to pollute (1)
66. Doesn't capture the value of externalities (positive or negative) (3)

VI. Highest Vote Getters: "What's Good, What's Wrong" with current farm policy:

GOOD (votes)

- Planting flexibility (18) / Production flexibility (7)
- Voluntary incentives for conservation (13)
- Market oriented (13)
- Puts conservation dollars on working lands (13)
- Energy title (12)
- Reward good actors for conservation (CSP) (11)
- Safety net: good risk protection (10)/ stability for producers/income (9)

WRONG (votes)

- Payments inhibit innovation (15)
- Distorts land use (13)
- Payments capitalized into land values (12)
- Inadequate incentives for production of environmental benefits (10)
- Pass through of dollars to other asset owners (9)

Small-Group Discussion Outputs: Goals for Farm Policy & Payments

TABLE 1

(Bryan Petrucci, Ernie Joaquin)

I. Goals for Farm Policy

Maximize flexibility
Planting signals should come from market sources (not your gut)

A. "Safety Net"
   - Income protection (revenue assurance or Canadian program)
   - Risk insurance; savings accounts

B. Permanent buy-out of base (could take years to do this)
   - Tenant/landlord share in payment

Replace with new production support programs tied to national priorities
- Energy
- Environment
- Food Security
- Rural Development
- National Purchase of Development Rights program

Disaster crop insurance

Have to screen ideas for budget exposure and for politics. A = easier to account and B = harder to predict and administer but broader political appeal

Also have to evaluate projected impacts. A = protects farmers (but what else?), predictable, limited in scope (good ideas). B = more unknowns but perhaps better outcome, better targeted, needs a lot more technical capacity

II. PAYMENTS DISCUSSION

25 percent cut in subsidies

- #1 target is farm debt – pay down farm debt but no payment beyond budget
- Capital expenditures
- Farm operating costs

100 percent cut in subsidies (in order of what would happen)

- Farm debt – why pay down?
- Farm rental – not reduce acres, just rent rates
- Farm capitol expenditures
- Estimated 30 percent reduction in rental rates
- Increase in interest rates could significantly bring down land prices
- Low interest has increased land prices a lot more than farm programs

100 percent cut with 20 year buyout in lump sum (in order of what would happen)

- Pay down farm debt. Reduce risk. If young enough, buy more land
- Recapitalize – depends on age and tax structure
    - New equipment?
    - New infrastructure?
    - Possibility for a new enterprise
- Succession? Possible, but incentives are needed
- Non-farm Household spending
    - Difficult to isolate because it's part of cash flow
    - Less money for personal capital expenses
    - Go into debt a little more
    - Catch up in a good year/little impact
    - Have wife earn more

TABLE 2
(Brian Brandt/Sara Hopper)

I. Goals for Farm Policy

- Maintain flexibility
- Shift in government payments to produce environmental benefits (in green box)- new products and uses, stimulate innovation
- Encourage highest and best use
- Do away with three entity rule and track payments to social security number
- Comprehensive approach to risk management
    - Crop insurance
    - Farmer savings accounts (i.e. Canadian system) with tax incentives/match from federal government
- Investment in public research for public benefit

II. PAYMENTS DISCUSSION

25 percent cut in subsidies

- Lower impacts for some agricultural sectors
- May have to borrow short term
- Won't trade equipment as often
- Would not impact what we plant
- Land rentals would come down
- Overall, would not be as great an impact as changes to LDP would have
- Would not change household decisions
- Impacts operation more than household

100 percent cut in subsidies

- Land rates would definitely go down
- Sell land to pay down debt
- Impact ability to purchase capital equipment
- Big impact on standard of living/lifestyle choices
- Dramatic hit to net worth
- A lot of farmers would get out (mid-sized farms completely?)
- Better land may stay in agriculture
- Marginal land will exit
- Low debt farmers would not be as drastically impacted
- Overnight hit to agribusiness/no new investment in machinery

100 percent cut with 20 year buyout in lump sum

- We're feeling better now
- What would the landowner do if the buy-out bond went to the tenant?
- Would not have big impact in areas with a lot of like kind exchanges
- Invest in non-agricultural enterprises
- Pay down land debt
- Short term spike in land values (wait to buy more land until prices drop)
- Younger farmers will expand and invest
- Older farmers will pay down debt and put dollars towards retirement

TABLE 3

(Ed Young, Ann Sorensen)

I. Goals for Farm Policy

- Payments decoupled from production = flexibility
- Environmental amenities payment (CSP, filter strips) – based on outcomes of practices and is also voluntary
- Actuarially sound revenue-based insurance system (WTO compliant)
- Production flexibility
- Transition CSP and filter strip programs to outcome based conservation programs
- Let sugar go
- Pie in the sky: adjust county loan rates to each individual producer based on his or her adoption of conservation practices
- Keep direct payments as bargaining chip with other countries for market access
- Do away with counter-cyclical and guaranteed payments and distribute liberated funds to subsidize crop insurance
- Increase crop insurance flexibility with possibility of distributing subsidy to individual for self-insurance
- Energy title – include biomass
- Increase funding for research
- Rural development – economic incentives
- Get rid of payment limitations and rachet down direct payments and marketing loan rate

II. PAYMENTS DISCUSSION

25 percent cut in subsidies

[note: the table pointed out that we currently have record high farm income and that influences their answers]

- Give up expansion, capital purchases and servicing debt (capital purchases increase debt)
- Change in crops produced
- Operate older equipment
- Reduce cash rent rates, land rates will come down [table estimated a five year delay].
- Delay capital investments.
- Bottom end farmers will fall out, maybe at an accelerated rate.

100 percent cut in subsidies

- Fall out rate will escalate
- Crop patterns will change. Marginal lands will drop out.
- Will change how we manage.
- May bring more diversity back into agriculture.
- Strong rural economies could mitigate the impacts by supplying off-farm jobs

100 percent cut with 20 year buyout in lump sum

- More cattle
- Great retirement
- Land values would go up short term, may come down long term?
- Expand operations, re-invest in the land
- Rents go down on marginal land
- Better managers will thrive
- Development will buy up land more quickly unless we protect it through purchase of development rights programs

TABLE 4

(Jimmy Daukas/Anita Zurbrugg)

I. Goals for Farm Policy

Risk production/Safety net

- Expand program to livestock
- Make it adequate
- Should deal with disasters written into the law with dollars set aside
- Production versus price – keep counter-cyclical payments [$/unit?]

Research

- Publicly funded

Conservation programs

- Public demand for environmental benefits
- Threat of regulation
- Environmental enhancement
    - Cost-share
    - CSP-operator oriented <u>(not landowner)</u>
    - <u>Reward and offer incentives</u>
    - Migrate environmental enhancement programs to CSP (will happen automatically)
    - <u>Fully funded</u>, entitlement program
    - <u>Rename</u> (listener from Harkin)
    - Fold existing cost-share into CSP
    - Add <u>energy</u> into CSP (builds constituency) e.g. shift CRP acres into energy
    - Reward the same producers getting dollars now with new program

Funds for value-added innovation

- Funds for energy production, especially alternative energy projects
- Biomass (infrastructure needed)
- Reward for Innovations resulting in efficiencies (e.g. disaster)

Technical Assistance

- Dedicated funds
- Affects all of the other programs
- Not enough dollars to get job done but too much dollars for private sector to jump in

All programs need to comply with WTO agreements. All limited by budget constraints.

II. PAYMENTS DISCUSSION

25 percent cut in subsidies

- A squeeze everywhere. Some producers may go out of business.
- 50 percent of the cut will be absorbed in costs on the front end
- Will hurt returns, less disposable income, less ability to reduce debt
- Those without debt will be affected less and in better shape to absorb the cut
- Less savings, no or reduced outside investment, no or reduced capital improvements, less likely to purchase machinery.
- Some will be forced to consider part time jobs, which may displace city cousins.
- Some effect in reducing land prices.

100 percent cut in subsidies

- Liquidate and move to Brazil.
- Farmers heavily leveraged and inefficient would be forced out. If the general economy is still strong at the time, producers would be able to recover more quickly.
- Farming will change from maximizing the dollars to be made through programs to lowering the cost of production as much as possible.
- Will force more diversity, drive cattle prices down.
- Machinery dealerships would be in free fall.
- Income shift from landowners to operators. Land values will go down except where development pressure supports the land prices. Land sales will increase.
- Marginal land not worth farming for crops.
- Those who have no or little debt will continue to buy land. Those highly leveraged will have to sell.
- Everyone will go no-till, even in Northern Illinois!

100 percent cut with 20 year buyout in lump sum

- Why not take it, especially if it is non-taxable? Those close to retirement would most likely jump at the chance.
- Landowners will take a hit, because one cannot easily separate land from the operation. If landowners somehow share in the benefit, they would not be hurt so drastically.
- Land prices influenced by development pressure are likely to be less affected.
- Rental rates will go down.
- Land would be sold at market price.
- Might eliminate 1031 exchanges, helping keep land prices down.
- Will park a lot of marginal land that won’t get farmed because of production. This will put more cows and sheep on some land, which may make sense.
- Opens up a scenario for land to be more economically used for energy production.

Notes from Table Discussions: Goals for Farm Policy & Payments

TABLE 1
(Bryan Petrucci, Ernie Joaquin)

I. Goals for Farm Policy

Design an alternative farm policy/program that keeps what is good and addresses what is wrong.

The group started deliberation on alternatives to current farm program that eliminate or reduce what the group identified earlier as "bad" characteristics or features and that maximize or enhance what they identified as "good" about the current set of farm programs. To do this, they referred to the condensed list of the five best and worst features of the farm programs.

At first, the group suggested that they identify goals for the next farm policy, such as providing maximum flexibility. Others suggested that they begin by identifying what are theoretical or practical goals for farm policy. The group discussed whether farm policy should aim for traditional revenue assurance or net income guarantee and what would be the consequences if they let the government buy out the base permanently. Should there be an intermediate step? The facilitator asked the group whether a policy that aims for safety net is mutually exclusive with a buyout policy. A participant shared that the dairy buyout experience showed that once they let people back in, it ruined the program.

The facilitator asked the group, 'If there is a buyout, would it open the door to other programs like the Conservation Security Program?' The group agreed and identified energy program as one potential beneficiary. The group liked the CSP concept but they said that the way it was implemented was watered down. The group also talked about national PDR programs and the role of states and their access to money. When the facilitator asked whether other incentive-based programs could happen without a government buyout, the consensus within the group was it could happen if the government could find the money. However, the budget deficit was identified as one of the biggest drivers of changes in the upcoming farm policy revision.

On the planting flexibility goal, the group decided that policy options should include a market orientation, conservation on working land, revenue assurance and some risk protection. The energy title in the farm bill was seen as particularly positive.

The group wanted to know more when someone suggested what a modified New Zealand program would look like. A participant posed the idea of a buyout with a safety net, but another suggested that a market-oriented system is not politically feasible at the moment.

At this point the facilitator identified two streams of proposals coming from the group: one is the traditional farm policy that guarantees a safety net, and other entertains the idea of a buyout (see flip chart). To find out how these two streams would promote what's good in farm policy and reduce what is bad, the group checked the items on the 'good' and 'bad' list. They noted that the permanent buyout would mostly solve the problems on the 'bad' list. Some type of insurance is part of either proposal (or of both). One participant noted that in order to make disaster insurance politically predictable, the policy proposal should provide for an act (vote) on the part of Congress, to get it on the budget.

The participants agreed that the buyout proposal has more unknowns and is harder to predict but is perhaps a better program, more efficient, and one that could target outcomes more carefully in theory. It also provides more outcomes. The traditional farm policy goal of safety net and revenue assurance, on the other hand, protects farms but at the expense of other programs. It has continuity, is more predictable, easier to account for and administer, and limited in scope.

Bryan's formal report to the plenary:

"We tried to focus our special discussion around really looking at the important issues we have identified in the 'good' and 'bad' things about farm programs. But before we did that, we believe that as far as the goals for the future farm bill are concerned, we identified maximum flexibility and finding signals from market sources not public sources as really critical items. Those things are very important.

We came up with sort of two separate but tied approaches, first is essentially the safety net approach – Approach "A" that has income protection, risk insurance, basically still providing support for the production of commodity crops but trying to do it more efficiently and maybe possibly cheaper.

Second, looking at this other idea – Approach "B" of tying or linking a permanent buyout of base to do away with the permanent payment system. And then tying new supports – production support programs tied to other national priorities – such as energy, environment, food security and rural development.

Looking at the things that we said, the cost of this buyout and the costs of the new programs need to be carefully considered. The buyout of the base needs to be included in the cost of these programs. Things like crop insurance and disaster insurance may be parts of this as well. An idea was even brought up of some type of a national PDR program. Maybe some of these national priority programs could be based on participation in such a program. There was a discussion that this buyout is supposed to take years to implement.

Either one of these two approaches would be a doable approach. To get them done, the three things you have to look at are the budget exposure of either approach, the politics of either approach, and evaluation of the projected income. There was some consensus that the "A" approach, the safety net approach, would certainly be easier to account for budgetarily and that "B" would be harder to predict, dollar-wise. Administration-wise, B would certainly be a different program to administer from what we currently have.

On the political side, the buyout coupled with other programs would have a broader appeal to the public than the traditional approach. From the evaluation and impact side, the buyout and related programs approach would have more unknowns but perhaps better outcomes. It could also be better targeted to a whole lot more issues that would appeal to American taxpayers. But, it will exact a lot more technical capacity in USDA and groups to carry something out before we achieve those outcomes.

Approach A would protect farm farmers, would put together programs that would help support farmers and protect incomes, but what else? That is the question: what else could we get out of that? It could be a very predictable program but limited in scope and limited in many of the good ideas that we would like farm programs to be."

Q & A with the Red Group:

- *On how these ideas should be carried out*. - We didn't talk about the tools to carry these out, other than the fact that we said this could take a long time. From a financial standpoint, what is the possibility of doing this instead of doing it in a phased-in approach, shifting money from commodities to buyouts over a number of years? There was some discussion, but we were not sure how it is playing out, with the Canadian approach with the revenue insurance or the savings account. We were not really sure what their experience is up to now, could that be some kind of a model? And with regards to the safety net, we were talking about the counter-cyclical and fixed payments approach to up the level of support for revenue assurance to offset some of the problems that we have the past few years.
- *On how much the buyout would cost*. - You mean, do we have any estimate? That's possible. We have an inner committee working on it (laughter). No, we project about $725 billion. Give or take. Over a three and a half year period.
- *On what is the mix between buyouts and what's left. What are you proposing to buyout?* - Any money or payments that are tied to the land. Then we have to farm several acres, of course, probably through a bidding process. This is not a new concept because the third bid for the CRP let you sell some of it. So the safety net is not connected to the base anymore. How are we going to pay for it? LDP and CCC loans – is the safety net. It's on production. Buyout is the direct payment. Is it mandatory? No, it's a volunteer program (laughter).
- <u>*On whether the group sees these – A and B- working together*</u> – No, there is not enough money to do both, it's one or the other. There was a lot of discussion on where the money is going to come from and part of the issue is that this permanent buyout and the second phase of this new production support programs is very

expensive. Where is that money going to come from? The hope is that over time, as you bought and phased out the subsidies in three to five years, then you'd attempt to look at non-revenue neutral sources for the money.

- *On whether the group would do a buyout and then start a new program* – No, maybe a new set of programs, not just based on program support but on other national priorities like energy, environment, food security and rural development. Same recipients.
- *On whether it would be capped or a regular income-* (laughter) – We did talk about landowners' interests and who would get the money from a buyout. We were concerned that landowners would enter the buyout to get the payment and the tenant would be forced off the land without getting anything. The solution proposed was if the buyout was $10 per acre, a landowner would get $7 while the tenant would get $3. This proposed split was about equity and fairness and sharing the benefits of a buyout plan.

II. PAYMENTS DISCUSSION

What would be the effect if policy dictated a 25% cut in direct and counter-cyclical payments?

What would be the effect if farm policy dictated a 100% cut in direct and counter-cyclical payments?

What if producers were offered a lump sum 20 year tradable bond, present value capitalized in compensation for counter cyclical and direct payments, tied to operator, not tied to land?

- The group notes that non-farm household spending is difficult to isolate because it is part of cash flow
- A 25 percent reduction would affect how they operate the farm by:
    - Paying down farm debt, but not ahead and not beyond their budget
    - Holding capital expenditures
    - Start trimming farm operating costs
- A 100 percent cut would affect:
    - Farm debt – they will not pay down
    - Farm rental – they will not reduce acres, just the rent rates (an estimated 30 percent reduction)
    - Farm capital expenditures
- A 100 percent cut with buyout of a bond equal to the value of 20 years of benefits with CCC and direct payments would lead them to:
    - Pay down farm debt
    - Reduce their risks
    - If the farmer is young enough, may buy more land
    - Recapitalize – upgrade equipment, purchase new equipment although there are tax consequences for new machinery
    - New infrastructure possible for a new enterprise
    - Recapitalizing depends on farmer's age and tax structure and a lot of personal factors, such as succession issues
    - The facilitator suggested looking at the New Zealand program to encourage beginning farmers

TABLE 2

(Brian Brandt/Sara Hopper)

I. Goals for Farm Policy

Design an alternative farm policy/program that keeps what is good and addresses what is wrong.

Replace direct payments with payments rewarding environmental performance

- you would give the farmer the option of accepting a lower direct payment (lower than currently receiving) and doing nothing OR taking a higher payment in exchange for producing environmental benefits
- this would be outcome/performance-based, with higher and higher payments in exchange for greater and greater environmental benefits produced
- program similar to CSP – you'd reward existing good stewards while continuing to create incentives for greater environmental improvements

AND….

Phase out CCPs and LDPs and phase in alternative risk management tools, including:

- crop insurance (assuming certain improvements/expansion to existing crop insurance policies); and
- some kind of farm savings accounts, funded by both the farmer (encouraged by new tax incentives) and the federal government (which might make some sort of match to further improve/increase farmer savings)
- this account could be used for retirement but also drawn down in "lean years" – when prices fall and/or in the case of natural disaster
- similar to the Canadian system and/or Sen. Lugar's proposal
- critical that phase out/phase in occurs gradually to minimize disruption
- anticipate that some savings from phase-out of CCPs and LDPs will accrue to Treasury (because the federal match/tax incentives will be cheaper than existing payments) BUT that some of the savings will be redirected to….

New/increased public investment in RESEARCH

- critical that all ag-related research is not funded by private entities (e.g., agribusiness) and/or Congressional earmarks – public investment (perhaps through a competitive process) needed to insure that public needs (for environmental progress, healthy food, revitalization of rural communities, new energy sources, etc.) will be met by implementing what's learned from ag research

II. PAYMENTS DISCUSSION

What would be the effect if policy dictated a 25% cut in direct and counter-cyclical payments?

- Could maintain lifestyle
- Lower impacts for some farm sectors
- May have to borrow short-term (b/c farm income goes back to the farm – off-farm income supports lifestyle)
- Won't replace equipment as frequently (group agrees land values will probably come down so that will partially offset the cut in payments)
- Overall, would not be as significant as change to LDPs would be
- They think prices would not stay as low for as long b/c planting decisions would change w/ low prices whereas they don't now

What would be the effect if farm policy dictated a 100% cut in direct and counter-cyclical payments?

- Land values would definitely drop
- Might have to sell some land (but note w/ drop in value, NOT a good time to do that)
- This could affect standard of living AND ability to purchase capital equipment
- Dramatic hit to net worth
- Lots of farmers would get out (mid-sized farms would be especially hard-hit)
- Better land may stay in ag – fewer farmers, bigger farms)
- Marginal land out of farming
- Low debt farmers would be less hard-hit
- Overnight hit to ag/rural business (farmers buying less equipment)

What if producers were offered a lump sum 20 year tradable bond, present value capitalized in compensation for counter cyclical and direct payments, tied to operator, not tied to land?

- We're feeling better now
- What would landowners do if $ goes to tenants (cash rent situation)
- Would not have big impact in areas w/ lots of like kind exchanges
- Invest in non-ag enterprises
- Pay down land debt
- Younger farmers will expand/invest
- Older farmers would put $ toward retirement

TABLE 3
(Ed Young, Ann Sorensen)

I. Goals for Farm Policy

Design an alternative farm policy/program that keeps what is good and addresses what is wrong.

1. Maximize flexibility (payments decoupled from production)
   - Payments related to public goals and attributes instead of production.
   - Use marketing concepts to determine how much the public is willing to pay for <u>outcomes</u>
   - Require farm plans, maybe tied to an environmental benefits index
   - Needs to be simple, something to measure. Remove subjectivity. A good model may be filter strips or a CSP-type program. Base payments on outcomes and make the program voluntary.
   - Maybe establish a point system for everything you use on the farm (nutrients, pesticides, practices). The system would have to regionally based.
   - How do we set a market for environmental amenities?
2. Actuarially sound, revenue-based crop insurance
   - Redesign crop insurance. Look at a Conservation Security Program type of program.
   - Reduce production payments over time and shift to conservation.
   - Get rid of all payments except marketing loan and LDPs.
   - Raise county loan rates. Adjust the rate for individual farmers based on their adoption of conservation practices. In other words, have a county loan rate adjusted to each farm's conservation security practices. Do away with countercyclical and guaranteed payments.
   - Reduce premiums based on risk.
   - If you don't use the crop insurance subsidy, you should be able to apply it to something else. If the insurance is actuarially sound, you should be able to transfer the subsidy. This would give you more flexibility to maybe insure some land at 50 percent, some at 85 percent depending on your perception of risk. You could use the subsidy for crop insurance and self-insure using the options market, marketing loans.
   - WTO compliant
3. Keep direct payments as a bargaining chip for the World Trade Organization. Reduce the payments as we gain market access. Bring down marketing loans as well. We can write the schedule of percent reductions in exchange for percent market access into the farm bill.
4. Energy title – including all forms of biomass.
5. Rural economic development. Recognize that farmers are now more dependent on the health of rural economies than vice versa.

6. Get rid of payment limitations, rachet down direct payments and marketing loan rates. Good conservation is profitable. However, we will lose control of producers when we have higher market prices. The better land will participate more in direct government payments (LDPs and market support). Poorer land will go into producing environmental benefits (as long as we keep up with technologies). Any CSP-type program must be flexible enough to incorporate technological advances.
7. Change won't be immediate. We need some way to transition and shift policy objects.
    - Expand producer group that benefits from programs
    - Improve safety net
    - Offer more assistance for indirect benefits (prescriptive research that provides more public benefit, new technology, technology assistance)
    - Prove flexibility
    - WTO compliant – consistency and leverage

II. PAYMENTS DISCUSSION

What would be the effect if policy dictated a 25% cut in direct and counter-cyclical payments?

[Note: the table pointed out that we currently have record high farm income and that influences their answers]

- Give up expansion, capital purchases and servicing debt (capital purchases increase debt)
- Change in crops produced
- Operate older equipment
- Reduce cash rent rates, land rates will come down [table estimated a five year delay]. It was pointed out that between 1998-2002, Illinois farms averaged $30,000/year on the farm. Net worth was static but cash rents continued to go up.
- Put off capital investments.
- Farmers are not good at managing numbers. The bottom end farmers will fall out, maybe at an accelerated rate. The good ones will always get the money.

What would be the effect if farm policy dictated a 100% cut in direct and counter-cyclical payments?

- Fall out rate will escalate
- Crop patterns will change. Marginal lands will drop out.
- Will change how we manage.
- May bring more diversity back into agriculture.
- Look at the period between 1998-2002 for answers. How many farmers downsized and got off-farm jobs?
- Off-farm jobs may be few but strong rural economies could mitigate the impacts

What if producers were offered a lump sum 20 year tradable bond, present value capitalized in compensation for counter cyclical and direct payments, tied to operator, not tied to land?

- More cattle
- Great retirement
- Land values would go up short term, may come down long term?
- Expand operations, re-invest in the land
- Rents go down on marginal land
- Better managers will thrive
- Development will buy up land more quickly unless we protect it through purchase of development rights programs

TABLE 4
(Jimmy Daukas/Anita Zurbrugg)

I. Goals for Farm Policy

Design an alternative farm policy/program that keeps what is good and addresses what is wrong.

Risk production/Safety net

- Producers can't handle risk by themselves, but do not expect risk in agriculture to be completely removed
- Expand program to livestock and to all enterprises for producers.
- Make it adequate and equitable to divvy benefit between landowner and operator.
- Make risk protection affordable, tie into regional/local actuarial tables.
- Address disasters written into farm policy with dollars set aside and allocated for such, to reduce political component of distribution.
- Production versus price – may need to keep a counter-cyclical component.
- Expand farmer safety net to include non-cash support, such as more research, more technology, technical assistance

Research

- Publicly funded preferred over private, cost of private research is incorporated into price of seed, chemicals, equipment.
- Differentiate between basic and applied, technical research. Public funding more critical for basic research.

Conservation programs

- Public demand for environmental benefits makes this more politically palatable for public support
- Threat of regulation will make farmers more willing to change.
- Move from environmental enhancement to a CSP type program.
    - Cost-share and/or reward, offering incentives. Fold existing cost-share into CSP
    - Flexibility, as long as operator is improving land environmentally, operator should be able to make decisions how to meat performances, land out of production should be able to be used for something else, such as grazing.
    - CSP-operator oriented (not landowner)
    - Fully funded, entitlement program
    - Rename to include more public palatable program such as Energy Security Program" (listener from Harkin)
    - ENERGY - Revitalize CSP with energy component (builds constituency) e.g. shift CRP acres into energy

- Reward the same producers getting dollars now with new program, cut out as many "losers" as possible Example: As CSP exists today, if we moved to all CSP type system $19 Billion would move from IL producers to other producers.
- Pay for environmental benefits that are not recognized within the market system.

Reward for value-added innovation

- Funds for energy production, especially alternative energy projects, ie: provide for storage support for ethanol production, incorporate wind energy systems into grid,
- Biomass, waste utilization (local infrastructure needed)
- Reward for innovations resulting in efficiencies (e.g. disaster) or cost share for trial and error

Technical Assistance

- Provide dedicated funds for all programs
- Presently: Not enough dollars to get job done but too much public dollars are provided for private sector to have incentive to jump in
- Provide up-to date technical training that can be delivered upon demand in a timely fashion

<u>WTO</u>   All programs need to comply with WTO agreements, and all are limited by budget constraints.
<u>Recipients of Program Funds</u>: Re-route funds in existing program to maximize the greatest number possible of present recipients to still be eligible to receive program funds.

II. PAYMENTS DISCUSSION

What would be the effect if policy dictated a 25% cut in direct and counter-cyclical payments?

This would create a squeeze everywhere, but the general consensus of the group seemed to indicate most producers at the table would overcome it. However, more producers back in the home community may be more significantly affected; some may go out of business. Some estimated fifty percent of the cut would be absorbed in costs, on front end. It will hurt returns; there will be less disposable income, and less ability to reduce debt for producers. Those without debt will be affected less and in better shape to absorb the cut.

There will be less ability to save, no or reduced outside investment, and no or reduced capital improvements. Producers will be less likely to purchase machinery. Some will be forced to consider part time jobs, which may displace city cousins.
This cut most likely will have some effect in reducing land prices, not drastic.

What would be the effect if farm policy dictated a 100% cut in direct and counter-cyclical payments?

"I'll liquidate and move to Brazil."

All the effects stated in the 25% scenario would be exaggerated. Machinery dealerships would be in free fall. Even then, farmers may be forced to consider leasing programs for machinery instead of purchasing. Farmers heavily leveraged and inefficient would be forced out. Those depending most on government payments will be hurt most as a group. Only a couple in the group indicated they would probably get out of business, and that would depend primarily on how drastically land prices were affected. If the general economy is still strong at the time, producers would be able to recover more quickly.

Farming will change from focusing on maximizing the $$ to be made through programs to focusing on lowering the cost of production as much as possible. Producers will cut as many input costs as possible.

It would force some kind of diversity in farming. Farmers would consider growing unsupported or new crops that they normally would not consider. Growers would consider getting back into livestock. It would therefore drive cattle prices down.
"Everyone will go no-till, even in Northern Illinois!"
All the effects stated in the 25% scenario would be exaggerated. Machinery dealerships would be in free fall. Even then, farmers may be forced to consider leasing programs for machinery instead of purchasing.

There would be an income shift from landowners to operators because land prices will fall. Land values will go down in all areas except where development pressure supports the land prices. Land sales will increase, however land will not go unfarmed in the heartland, because variable costs would be below existing costs, and the good productive land will be worth farming. Marginal land will not be worth farming for crops.

What affect will it have on landowner investments or landlords? Those who have no or little debt will continue to buy land. Those highly leveraged will have to sell.

What if producers were offered a lump sum 20 year tradable bond, present value capitalized in compensation for counter cyclical and direct payments, tied to operator, not tied to land?

"Why not take it, especially if it is non-taxable?" Young producers may look at this differently, with more reservation than older producers. Older producers, those close to retirement, would most likely jump at this opportunity.

In this Buyout scenario, landowners would take a hit, because one cannot easily separate land from the operation. This may be a necessary in some manner because land prices are over inflated. Land prices influenced by development pressure are likely to be less affected. Rental rates will also go down and land would be sold closer to market price. This scenario may reduce the use of 1031 exchanges, which may also help to mitigate inflated land prices.

"Bringing land prices down is the key to market survival."

If Buyout was structured to allow landowners to somehow share in the benefit of the Buyout, then landowners may not be hurt so drastically. However, if one compares this type of market adjustment to the way the stock market operates, landowners who have used land as an investment would take a loss and then benefit from the tax write off.

The Buyout would park a lot of marginal land that won't get farmed because of production. This will put more cows and sheep on some land, which may make sense. It also opens up a scenario for land to be more economically used for energy production. The energy question or issue, and how it is being dealt with within US policy can make a big difference in how this might play out.

GENERAL DISCUSSION NOTABLE POINTS

Rural Development Issue
Group consensus that rural development is critical to agriculture, but no consensus as to what extent RD should be addressed within farm policy. Warfield: "Farm income is more dependent on a strong rural economy than a strong rural economy is dependent on farm household income."

2007 will be a transitional farm bill, toward free market economy.

Need to avoid rewarding agricultural inefficiencies, but reward efficiency and innovation.