

Chapter 4

General Effects of Current Payment Limitations

This chapter examines the economic effects of current payment limitations and the taxpayer and producer costs of administering payment limits. The chapter also discusses the effects of permitting producers to use commodity certificates to obtain marketing assistance loan benefits. At the time this study was prepared, the FSA could not provide the Commission with information on the number of producers affected or the reduction in payments resulting from the 2002 Act's payment limitations on direct payments, counter-cyclical payments, loan deficiency payments, and marketing loan gains. To estimate the effects of current payment limitations, the Commission relied on PFC payment data provided by the FSA for the 2000 and 2001 crops. In both years, PFC payments, which correspond closely to the 2002 Act's direct payments, were limited under the 1996 Act to \$40,000 per person, the current limit on direct payments.

The effects of payment limitations on direct payments, counter-cyclical payments, loan deficiency payments, and marketing loan gains depend on the extent to which the limitations reduce payments to producers and the extent to which producers, who have payments reduced because of the limits, restructure their farming operations to avoid the reduction in payments. The FSA tracks and reduces payments when payments would otherwise exceed the payment limitation.

Total Reduction in Payments

The 1996 Act authorized \$4.190 billion in PFC payments for the 2001 crops. In that year, 5,929 or 0.5 percent of the 1,177,366 producers (persons actively engaged in agriculture) receiving PFC payments had payments reduced because of the \$40,000 limit on PFC payments (table 4.1). Producers reaching the payment limit had payments reduced by \$38 million or the payment limitation reduced total payments by 0.9 percent. On average, each producer reaching the payment limit had payments reduced by \$6,422 (appendix table 4.2).

Direct payments are projected to total about \$5.2 billion annually for the 2002-07 crops. For the 2000 crops, the 1996 Act authorized almost \$5.2 billion in PFC payments and these payments were also limited to \$40,000 per person. In 2000, 1,215,706 producers received PFC payments and 12,298 or 1 percent of producers had payments reduced because of the payment limit (table 4.1). On average, each producer reaching the payment limit had pay-

Table 4.1 Payment reduction and producers affected by the \$40,000 payment limitation on PFC payments

	2000 crops	2001 crops
Payments reduced, dollars	\$82,648,742	\$38,078,198
Payments made, dollars	\$5,066,319,393	\$4,101,876,505
Percentage reduction	1.6	0.9
Producers reaching limit	12,298	5,929
Total producers	1,215,706	1,177,366
Percentage of producers affected	1.0	0.5

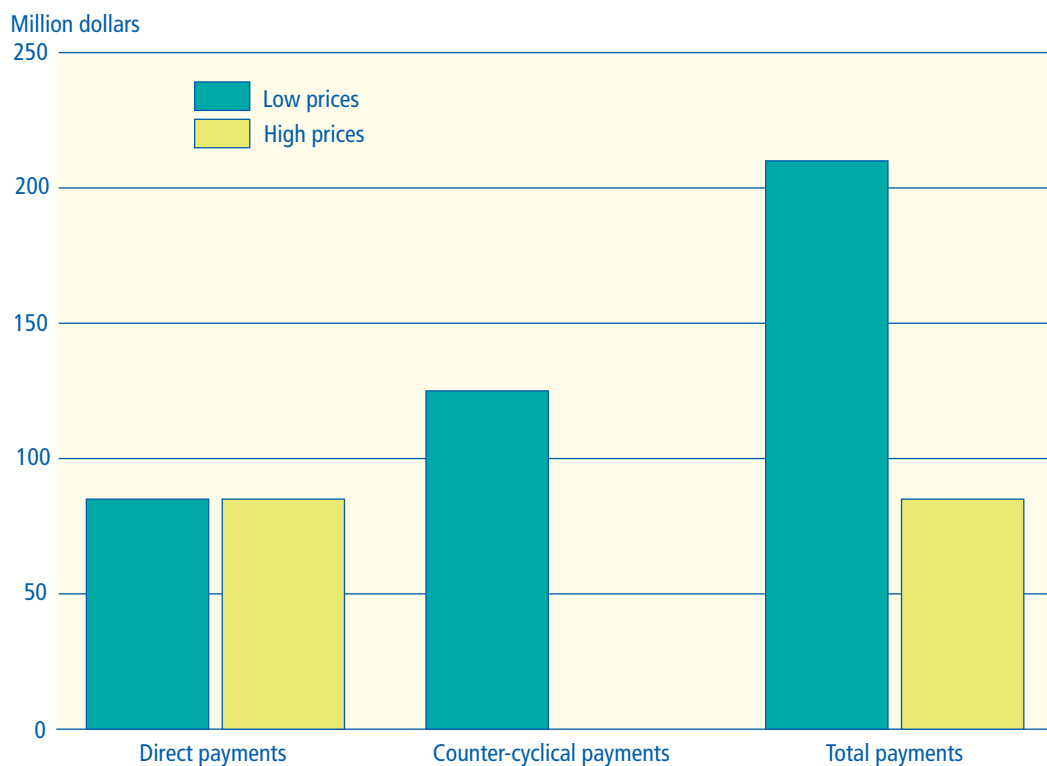
Source: USDA Farm Service Agency

ments reduced by \$6,721 and total payments were reduced by \$83 million or 1.6 percent (appendix table 4.1). Since the 2002 Act has a \$40,000 limit on direct payments and direct payments are projected to total \$5.2 billion, the payment limitation on direct payments is also expected to reduce payments by about 1.6 percent or about \$85 million per year, assuming producers who reach the payment limit do not restructure further.

The extent to which the \$65,000 limitation on counter-cyclical payments lowers payments to producers depends on the size of the payments, which varies depending on market prices. When market prices are high, direct payments will likely exceed counter-cyclical payments. For example, direct payments are projected to exceed counter-cyclical payments for the 2002 crops by \$3.5 billion. Since the payment limit on counter-cyclical payments is \$65,000, compared with \$40,000 for direct payments, the payment limit on counter-cyclical payments is expected to result in less reduction in payments than the payment limit on direct payments when direct payments exceed counter-cyclical payments. This relationship is expected to hold even though, under the 2002 Act, producers updating base acres could also elect to partially update payment yields for counter-cyclical payments. No updating of payment yields was permitted for direct payments under the 2002 Act.

If market prices for all eligible crops fall to or below the loan rate, counter-cyclical payments could reach nearly \$8 billion annually for the 2004-07 crops, greatly exceeding direct payments of \$5.2 billion. Combining the effects of the larger payments with the higher limit, the number of producers whose payments are reduced and the percentage reduction in

Figure 4.1. Estimated reduction in direct and counter-cyclical payments (current payment limits)



Source: Commission estimates

counter-cyclical payments is expected to be very similar to the number of producers whose payments are reduced and the percentage reduction in payments because of the \$40,000 limit on direct payments. Furthermore, it is very likely that many of the same producers would have both their direct and counter-cyclical payments reduced under low prices.

The possible impact of current payment limits is shown in figure 4.1. The payment limit on direct payments could reduce payments by about \$85 million, with about 1 percent of producers having payments reduced. In addition, the payment limit on counter-cyclical payments could reduce payments by about \$125 million affecting about 1 percent of producers. When prices for eligible crops move above each crop's loan rate, fewer producers would reach the \$65,000 limit on counter-cyclical payments and the reduction in payments could be much less.

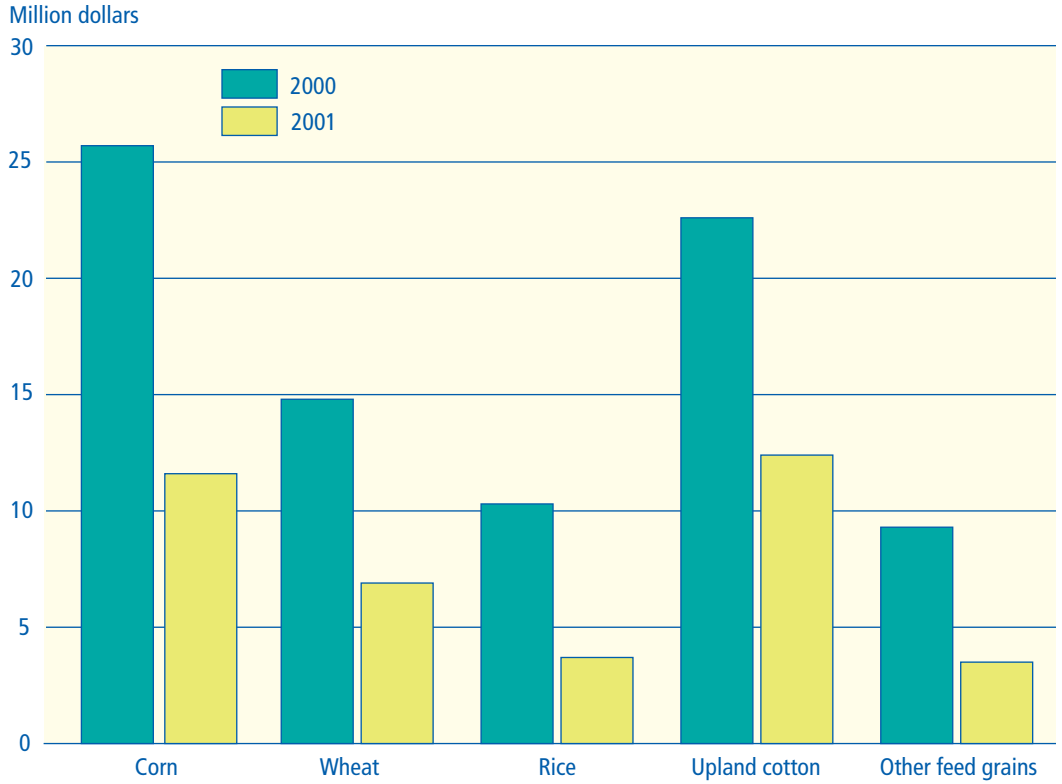
The 2002 Act limits loan deficiency payments and marketing loan gains to \$75,000 per person. However, there is no limit on marketing loan benefits realized through the use of commodity certificates or through the forfeiture of marketing assistance loans. Thus, the current payment limit on loan deficiency payments and marketing loan gains does not reduce the amount of marketing loan benefits a producer may receive.

Reduction in Payments by Commodity

In 2000, the \$40,000 limit reduced upland cotton PFC payments by \$22.6 million and rice PFC payments by \$10.3 million (figure 4.2). The reduction in payments amounted to 3.8 percent of total payments allocated for upland cotton and 2.3 percent of payments allocated for rice (appendix table 4.5). The limit reduced PFC payments for wheat by \$14.8 million and lowered corn payments by \$25.7 million, the most of any commodity in 2000. For these two crops, the reduction in payments amounted to 1.1 percent of PFC payments allocated to each. PFC payments for other feed grains (sorghum, barley, and oats) were reduced by \$9.3 million in 2000. The reduction in payments averaged 2.5 percent of total PFC payments for the three crops. Many of these producers likely had payments reduced because they also received payments for other crops, such as wheat or corn.

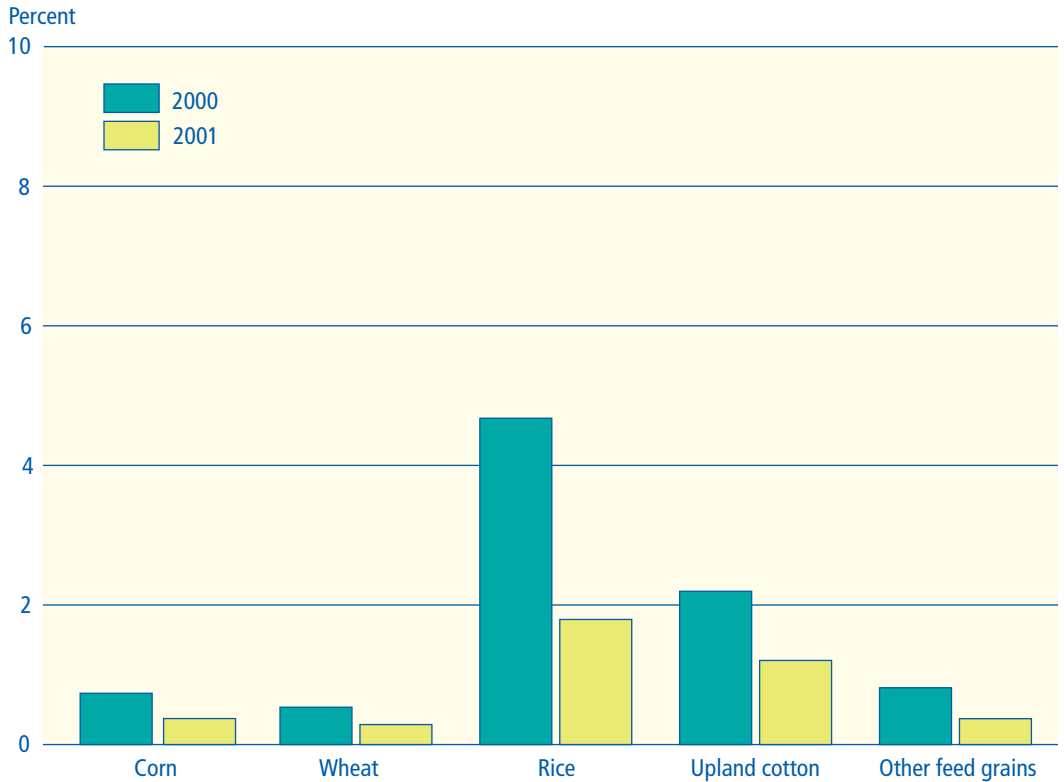
In 2001, the limit on PFC payments resulted in a smaller drop in payments for all crops, as the decline in PFC payments of about \$1 billion from the previous year caused fewer producers to reach the payment limit. In 2001, the payment limitation lowered upland cotton and rice PFC payments by \$12.4 million and \$3.7 million, respectively (appendix table 4.6). PFC payments for upland cotton were reduced by 2.5 percent and payments for rice were lowered by 1.1 percent, while payments for corn and wheat each were reduced by 0.6 percent in 2001. PFC payments for corn and wheat were lowered by \$11.6 million and \$6.9 million, respectively, because of the limit on PFC payments. Payments for sorghum, barley, and oats were reduced by \$3.5 million or 1.2 percent.

Figure 4.2. Reduction in PFC payments by commodity (\$40,000 limit)



Source: USDA Farm Service Agency

Figure 4.3. Percentage of producers having PFC payments reduced (\$40,000 limit)



Source: USDA Farm Service Agency

Payment limits tend to lower payments to a higher percentage of producers receiving upland cotton and rice payments than producers receiving payments for other crops (see appendix tables 4.3 and 4.4 for the number of producers receiving payments by crop). In 2000, the \$40,000 PFC limit reduced payments to 0.7 percent of producers receiving corn payments and 0.5 percent of producers receiving wheat payments (figure 4.3). For sorghum, barley, and oats, from 0.3 to 1.3 percent of producers receiving PFC payments for those crops had payments reduced. In contrast, 2.2 percent of the producers receiving upland cotton and 4.7 percent of the producers receiving rice PFC payments had payments lowered in 2000 because of the payment limit. In 2001, 0.3 percent of the producers receiving wheat and 0.4 percent of the producers receiving feed-grain payments had payments reduced, while 1.2 percent of the producers receiving upland cotton payments and 1.8 percent of the producers receiving rice payments had payments lowered because of the \$40,000 limit on PFC payments.

Direct payment rates for wheat, feed grains, upland cotton, and rice are between the 2000 and 2001 crop PFC payment rates. As a result, the reduction in payments in 2000 and 2001 because of the \$40,000 limit on PFC payments can be used to approximate the expected reduction in payments for those commodities resulting from the \$40,000 limit on direct payments, assuming producers reaching the payment limit do not restructure further. For the 2002-07 crops, the payment limit on direct payments is projected to reduce payments for corn by about \$15 million, other feed grains by about \$7 million, wheat by about \$10 million, rice by about \$7 million, and upland cotton by about \$20 million.

The above estimates understate the loss in direct payments due to the payment limitation, because the 2002 Act made soybeans, other oilseeds, and peanuts eligible for direct payments and these payments are also subject to limits. For soybeans and other oilseeds, direct payments for these crops will be combined with direct payments for wheat, feed grains, rice, and upland cotton to determine whether payments exceed the \$40,000 limit. Direct payments on peanuts are subject to a separate limit of \$40,000. Therefore, more producers growing oilseeds will be subject to payment limits than in the past. Making direct payments on soybeans, other oilseeds, and peanuts subject to payment limits is projected to reduce payments for the 2002-07 crops by about \$25 million annually, leading to a total reduction of about \$85 million annually in direct payments because of the \$40,000 payment limitation.

As indicated earlier, the \$65,000 payment limit on counter-cyclical payments is expected to lower total counter-cyclical payments by as much as \$125 million, if prices for all eligible crops fall below each crop's loan rate. Maximum counter-cyclical payments per base acre were compared to direct payments per acre to arrive at estimates of the reduction in counter-cyclical payments by crop due to the \$65,000 limit on counter-cyclical payments. Adjustments were made to account for differences in the payment limits and payment yields for direct and counter-cyclical payments.

Under a low-price scenario, the \$65,000 payment limit is projected to lower counter-cyclical payments by as much as \$3 million for sorghum, barley, and oats, \$3 million for rice, \$10 million for wheat, \$32 million for corn, and \$60 million for upland cotton. Including the

counter-cyclical payments that will be paid for oilseeds, the \$65,000 limit could further reduce counter-cyclical payments by an additional \$10-\$20 million, if the prices for all crops eligible for counter-cyclical payments fall below each crop's loan rate. Compared with direct payment rates, maximum counter-cyclical payment rates are much higher for corn, oats, upland cotton, and peanuts. When prices are low, the limit on counter-cyclical payments will lead to a greater reduction in payments for corn, oats, upland cotton, and peanuts than the limit on direct payments. For the remaining crops eligible for direct and counter-cyclical payments, the payment limit on direct payments is expected to lead to a greater reduction in payments than the limit on counter-cyclical payments.

A higher percentage of rice and upland cotton producers have their payments reduced because of payment limitations for two reasons. First, rice and upland cotton farms tend to be larger than wheat, oilseed, and feed-grain farms and, since direct and counter-cyclical payments are based on historical production (base acres times program yield), payments increase with farm size. According to the 1997 Census of Agriculture, farms producing rice harvested on average 336 acres of rice and farms producing upland cotton harvested on average 420 acres of upland cotton. In contrast, farms producing wheat, corn, and soybeans each averaged less than 240 harvested acres. In 1997, less than 10 percent of the farms growing corn,

Table 4.2. Distribution of farms by acres harvested, 1997

	1-49	50-99	100-249	250-499	500-999	1,000-1,999	2,000 or more
	Percent						
Corn	37.8	18.1	23.9	12.8	5.8	1.3	0.2
Sorghum	31.0	21.7	27.9	12.3	5.1	1.5	0.3
Barley	45.5	16.2	21.4	10.6	4.8	1.1	0.3
Oats	85.1	9.3	4.6	0.6	0.1	–	1/
Wheat	37.5	16.1	20.2	12.0	8.8	4.1	1.1
Soybeans	31.1	19.5	26.3	14.6	6.7	1.6	0.3
Upland cotton	15.0	11.8	23.4	20.9	18.7	8.2	1.9
Rice	8.9	9.9	31.1	30.3	15.4	3.7	0.8
Peanuts	46.5	19.2	22.6	8.2	2.8	0.5	¹

– Denotes less than 0.05 percent.

¹ Combined with previous category because of lack of data.

Source: 1997 Census of Agriculture

Table 4.3 Payments per base acre and base acreage of various crops needed to reach the payment limit on direct payments, 2002-07 crops

Crop	Unit	Payment rate, dollars per unit	Average program yield, per acre	Base acreage factor	Payment per base acre, dollars per unit	Base acres to reach \$40,000 payment limit
Corn	bushel	.28	102.7	.85	24.4	1,636
Sorghum	bushel	.35	57.0	.85	17.0	2,359
Barley	bushel	.24	46.6	.85	9.5	4,208
Oats	bushel	.024	50.6	.85	1.0	38,751
Wheat	bushel	.52	34.5	.85	15.2	2,623
Soybeans	bushel	.44	30.0	.85	11.2	3,565
Upland cotton	pound	.0667	600	.85	34.0	1,176
Rice	hundredweight	2.35	48.15	.85	96.2	416
Peanuts	ton	36	1.2	.85	36.7	1,089

Source: CCC estimates, FY 2004 President's Budget baseline

sorghum, barley, oats, soybeans, and peanuts harvested more than 500 acres of those crops (table 4.2). About 13 percent of the farms growing wheat harvested more than 500 acres of wheat but nearly one-fifth of the farms growing rice and over one-quarter of the farms growing cotton harvested more than 500 acres of those crops.

The second reason why a higher percentage of rice and upland cotton producers have their payments reduced is that payments per base acre tend to be higher for rice and upland cotton than for other commodities eligible for direct and counter-cyclical payments. For an individual producer, the payment per acre depends on the farm's program yield for each crop eligible for payments. Using estimates of national average direct payment yields as reported in the FY 2004 President's Budget baseline, direct payments average about \$96 per base acre for rice, \$37 per base acre for peanuts, \$34 per base acre for cotton, \$24 per base acre for corn, \$15 per base acre for wheat, and about \$11 per base acre for soybeans (table 4.3). As a result, it generally takes fewer acres of rice and upland cotton to reach the payment limitation on direct payments. In regions where program yields are above average, it takes fewer acres to reach the payment limitation than in regions with below-average program yields.

As with direct payments, counter-cyclical payments per acre vary widely from farm to farm and from region to region, reflecting differences in payment yields. Using estimates of national average counter-cyclical payment yields from the FY 2004 President's Budget baseline, counter-cyclical payments would average \$73 per base acre for upland cotton, \$79 per base acre for rice, and \$106 per base acre for peanuts, if market prices are at or below each eligible crop's loan rate (table 4.4). In contrast, counter-cyclical payments could average about \$40 per acre for corn, \$20 per acre for wheat, and \$11 per acre for soybeans under low prices.

Marketing assistance loan benefits per acre also tend to be higher for upland cotton and rice than for other commodities eligible for marketing assistance loans. For the 1999-2001 crops, marketing assistance loan benefits, including commodity certificate and forfeiture gains, averaged \$177 per harvested acre for rice, \$117 per harvested acre for upland cotton, \$38 per harvested acre for soybeans, \$29 per harvested acre for corn, and \$12 per harvested acre for wheat. The changes in loan rates under the 2002 Act could boost marketing loan benefits for

Table 4.4. Maximum counter-cyclical payments per base acre and base acreage of various crops needed to reach payment limit on counter-cyclical payments, 2002-07 crops

Crop	Unit	Maximum payment rate, dollars per unit		Average program yield per acre	Base acreage factor	Payment per base acre, dollars		Base acres to reach \$65,000 payment limit	
		2002-03	2004-07	2002-07	2002-07	2002-03	2004-07	2002-03	2004-07
Corn	bushel	.34	.40	127.7	.85	36.9	43.4	1,761	1,497
Sorghum	bushel	.21	.27	62.0	.85	11.1	14.2	5,873	4,568
Barley	bushel	.09	.15	55.7	.85	4.3	7.1	15,254	9,153
Oats	bushel	.026	.086	58.1	.85	1.3	4.2	50,623	15,305
Wheat	bushel	.54	.65	39.8	.85	18.3	22.0	3,558	2,956
Soybeans	bushel	.36	.36	36.3	.85	11.1	11.1	5,852	5,852
Upland cotton	pound	.1373	.1373	625	.85	72.9	72.9	891	891
Rice	hundredweight	1.65	1.65	56.32	.85	79.0	79.0	823	823
Peanuts	ton	104	104	1.2	.85	106.1	106.1	613	613

Source: CCC estimates, FY 2004 President's Budget baseline

corn by \$10 per acre, sorghum by \$16 per acre, barley by \$13 per acre, and wheat and oats by \$8 per acre, and reduce marketing loan benefits for soybeans by about \$10 per acre. Marketing assistance loan benefits per acre were left essentially unchanged under the 2002 Act for rice and upland cotton. Even though marketing assistance loan benefits vary from year to year depending on the level of market prices, marketing assistance loan benefits per harvested acre are projected to continue to be much higher for rice and upland cotton than for feed grains, soybeans, and wheat in most years. Marketing assistance loan benefits also vary widely from farm to farm and region to region reflecting differences in yields per acre across farms and regions of the country.

Generally, direct and counter-cyclical payment rates and marketing assistance loan benefits for the various crops eligible for payments reflect differences in production costs, with rice, upland cotton, and peanuts having higher payments and higher per-unit variable production cost than wheat, feed grains, and soybeans. For 2003, total support per base acre (the sum of direct payment, maximum counter-cyclical payment, and the loan rate) for corn amounts to \$2.42 per bushel or 193 percent of variable cost per bushel (table 4.5). For other feed grains, total support ranges from 145 to 164 percent of variable cost. Total support is equivalent to 218 percent of variable cost for wheat, 170 percent for peanuts, 259 percent for soybeans, 164 percent for upland cotton, and 186 percent for rice.

Table 4.5. Maximum support per base acre in relation to variable cost of production, 2003

Crop	Unit	Direct payment ¹	Maximum counter-cyclical payment ²	Marketing assistance loan rate	Total support	Variable cost	Direct payment divided by variable cost	Direct plus maximum counter-cyclical payment divided by variable cost	Total support divided by variable cost
		Dollars per unit					Percent		
Corn	bushel	0.17	0.26	1.98	2.42	1.23	14	35	193
Sorghum	bushel	0.25	0.16	1.98	2.39	1.54	17	28	164
Barley	bushel	0.15	0.07	1.88	2.10	1.43	11	15	145
Oats	bushel	0.02	0.02	1.35	1.39	0.86	2	4	153
Wheat	bushel	0.38	0.45	2.80	3.63	1.62	23	50	218
Soybeans	bushel	0.28	0.28	5.00	5.56	2.07	13	26	259
Upland cotton	pound	0.05	0.11	0.52	0.69	0.34	29	40	164
Rice	hundredweight	1.44	1.18	6.50	9.12	4.68	13	54	186
Peanuts	ton	27.39	79.13	355.00	461.53	0.11	10	39	170

Note: Direct and counter-cyclical payments are decoupled from production.

¹Direct payment rate adjusted for nonpayment acres and direct payment yield relative to projected yield.

²Counter-cyclical payment rate adjusted for nonpayment acres and counter-cyclical payment yield relative to projected yield.

Source: CCC estimates, FY 2004 President's Budget baseline and USDA Agricultural Baseline Projections to 2012

Reduction in Payments by State

In 2000, California producers reaching the \$40,000 limit on PFC payments had payments reduced by \$19.6 million (figure 4.4). A total of 1,146 California producers had their payments reduced by \$17,093 on average. Texas producers had PFC payments lowered by \$10.0 million. Reduced payments to upland cotton producers accounted for 60 percent of the reduction in payments in California and 35 percent of the payment reduction in Texas. The payment reductions in California and Texas represented 36 percent of the total reduction in payments across all States in 2000 and 39 percent in 2001.

Several other States had PFC payments reduced by \$3-\$5 million in 2000. Kansas had payments reduced by \$4.85 million, the third most of any State. In Kansas, 1,029 wheat, corn, sorghum, barley, and oats producers had payments reduced on average by \$4,711 in 2000 because of the limit of \$40,000 on PFC payments. The fourth leading State, Arkansas, had PFC payments reduced by \$4.03 million. Other States that had payments reduced by \$3-\$5 million in 2000

Figure 4.4. Reduction in PFC payments by State, 2000 (\$40,000 limit)

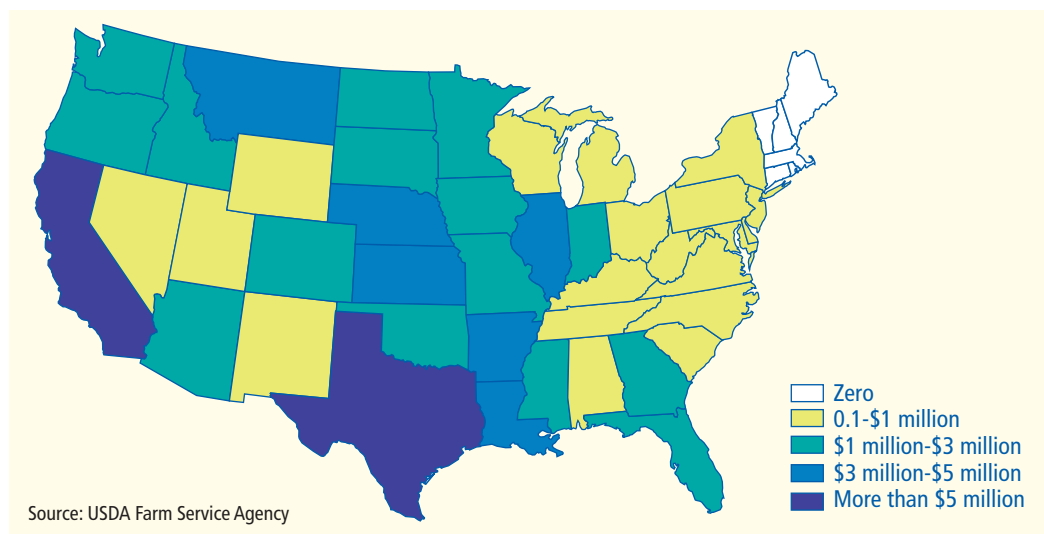
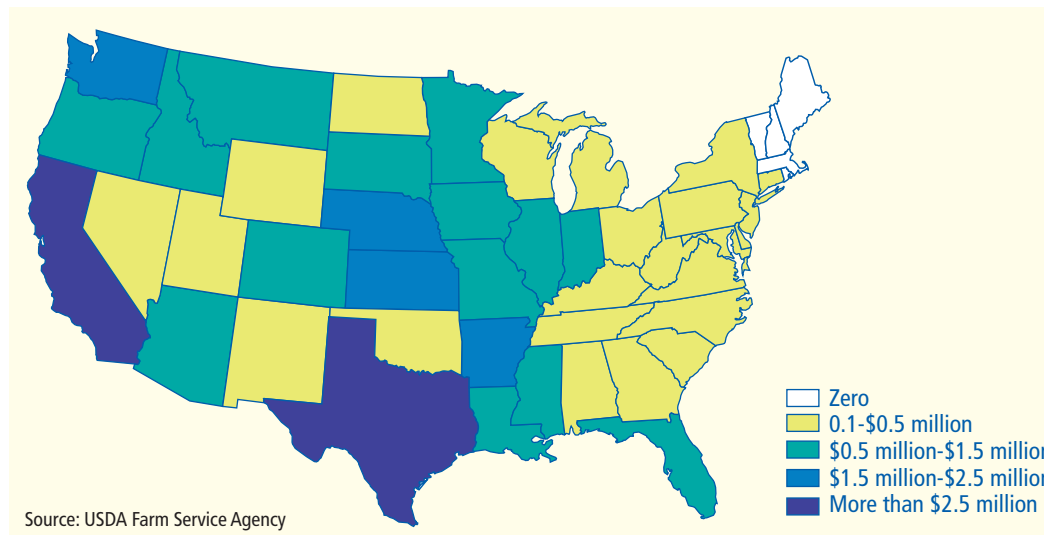


Figure 4.5. Reduction in PFC payments by State, 2001 (\$40,000 limit)



included: Nebraska, \$3.65 million; Illinois, \$3.45 million; Montana, \$3.11 million; and Louisiana, \$3.08 million. Generally, the relative ranking of States by the amount payments were reduced because of the \$40,000 limit on PFC payments holds for both 2000 and 2001 (figure 4.5).

Another measure of the relative effects of payment limits across States and regions is the percentage reduction in payments. Nationally, the \$40,000 limit on PFC payments reduced payments to producers by 1.6 percent in 2000 and 0.9 percent in 2001, but the percentage reduction in payments varied widely across States and regions (appendix table 4.3). In 2000, PFC payments to producers in Florida were reduced by 12.3 percent, the largest percentage reduction of any State (figure 4.6). Florida was followed by California (reduction of 9.7 percent), and Nevada (7.7 percent). In Nevada, 5 producers had their payments lowered an average of \$13,908. In 2000, the payment limit on PFC payments reduced payments by 3-5 percent in Arizona, Colorado, Delaware, and Oregon. For the most part, the States in which the percentage reduction in payments exceeded the national average for 2000 also had above-average percentage reductions in payments for 2001 (figure 4.7, appendix table 4.4).

Figure 4.6. Percentage reduction in PFC payments by State, 2000 (\$40,000 limit)

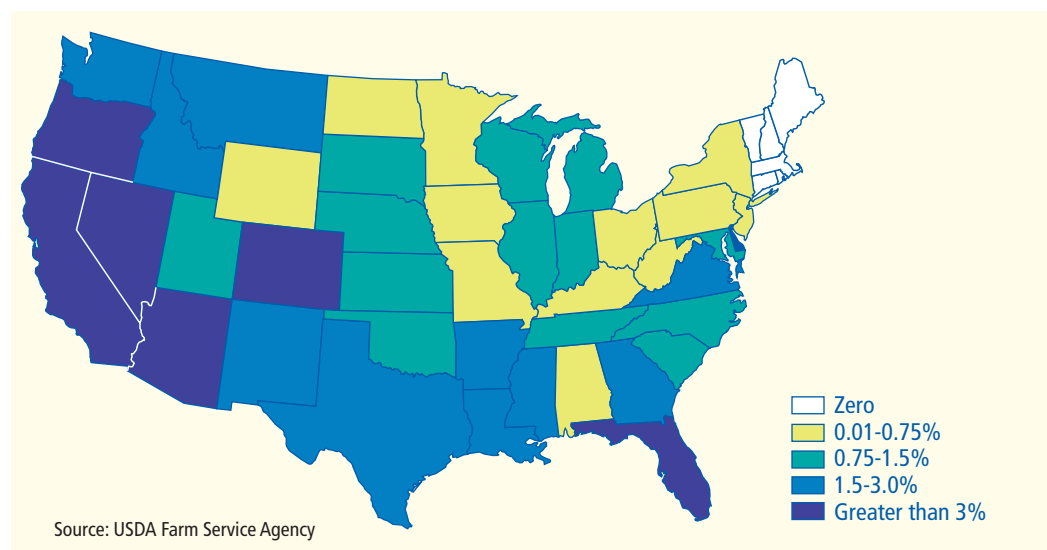
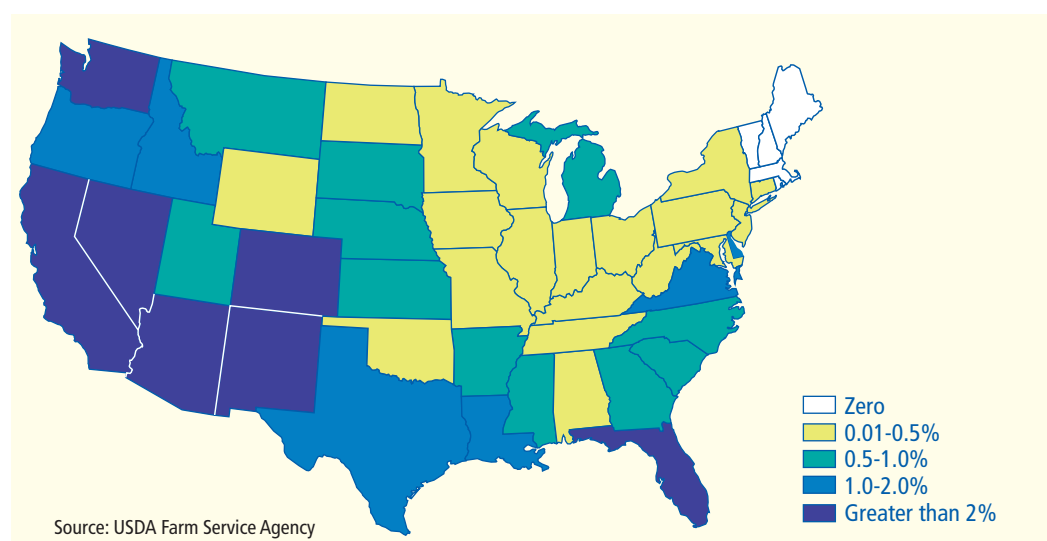


Figure 4.7. Percentage reduction in PFC payments by State, 2001 (\$40,000 limit)



While the above data support the conclusion that payment limits tend to result in a greater decline in payments in States and regions where upland cotton and rice production dominate, producers in other States and regions also are affected by payment limits. Producers in 42 States in 2000 and producers in 43 States in 2001 had payments reduced because of the \$40,000 limit on PFC payments. The producers affected by payment limits produce a variety of crops and are scattered throughout the primary wheat, feed-grain, rice, and upland cotton producing States and regions. Furthermore, making soybeans, other oilseeds, and peanuts eligible for direct and counter-cyclical payments under the 2002 Act is expected to increase the number of producers who have payments reduced because of payment limits in the Corn Belt and in other regions where there is a high level of concentration of production of these crops.

Farm Structure

The limited effects of current payment limitations on payments to producers may be due to the payment limits being set at a level at which few producers are affected. Alternatively, many producers may potentially be affected but may be able to reorganize their farming operation to limit the reduction in payments. There are several ways a farm may restructure under existing rules and qualify for additional payments. For example, the farm may add individuals or entities that are actively engaged in the farming operation with these additional persons qualifying for payments (see Chapter 2).

Restructuring of the farming operation in response to payment limits may also change the sharing of production and price risk between the landowner and the farm operator. An owner-operator reaching the limit on payments may decide not to create additional entities and instead cash rent or share rent a portion of the farm to someone else, shifting a portion of the risk to the renter. In this instance, the owner-operator may be able to capture a major portion of the payments that would otherwise be lost because of payment limits through a cash or share rental agreement. The ability of the owner-operator to capture payments by either cash or share renting would depend on the strength of the local land rental market and the extent to which government payments are bid into land rents.

The operator who rents land and reaches the payment limit may also reorganize the farming operation by adding additional individuals or entities that are actively engaged in the farming operation or switching from a cash to a share rental agreement. The acceptability of such a restructuring depends on the landowner's willingness and ability to handle risk.

Data on the size distribution of wheat, soybean, corn, rice, and upland cotton farms by State from the 1997 Census of Agriculture were used to provide an indication of the extent of farm restructuring and the amount of payments by crop that could be potentially affected by payment limitations. For each State, the number of acres needed for a farm to reach the payment limitation was determined by dividing the applicable payment limitation by the payment rate times the State average program payment yield for each eligible crop. Each farm was assumed to be operated by two eligible payment limit persons, doubling the payment

limitation for direct and counter-cyclical payments. Under these assumptions, the \$40,000 payment limitation on direct payments was estimated to reduce payments to program participants by about \$185 million annually, or 3-4 percent. In comparison, the FSA data indicate that payments are lowered by about 1.6 percent. This suggests that many farms are structured or have restructured to reduce the effects of payment limitations.

One way for farms to restructure to avoid payment limits is to increase the number of producers (persons actively engaged) in the farming operation, thereby increasing the amount of payments that a farm can receive. At the request of the Commission, the FSA provided data on the distribution of the number of producers (persons) on FSA farms. Nationally, 87.9 percent of FSA farms had 1-2 producers, 10.9 percent had 3-5 producers, 1.1 percent had 6-10 producers, and 0.1 percent of farms had 11 or more producers in 2002 (table 4.6). It is likely that many of the farms with a large number of producers are structured to lessen the effects of payment limits. In 2002, there were 325 farms with 21 or more producers. Ninety percent of these farms were located in 9 States—Arkansas, California, Illinois, Louisiana, Mississippi, Missouri, North Dakota, Texas, and Washington. In many instances, these same States were among the leading States in terms of the value of payments lost and the number of producers who had payments reduced because of the limit on PFC payments.

The current limitations on direct and counter-cyclical payments may discourage a small number of large producers from expanding. If a producer reaching the payment limitation on direct and counter-cyclical payments is limited in the ability to add additional persons that are actively engaged in the farming operation, the decision to expand would be based on the expected returns of owning or renting additional land, excluding those government payments that may be subject to payment limitations. If payments per acre are relatively low and make up a small portion of the purchase or rental value per acre, the decision to expand is probably less influenced by payment limitations.

A producer whose payments are restricted by payment limits could elect to expand by purchasing or renting cropland in which a small portion of the acreage is eligible for direct and counter-cyclical payments. Alternatively, the producer could purchase (or rent) land in which a high percentage of the land is eligible for direct and counter-cyclical payments, but the base acreage of the land purchased (or rented) applies to crops in which direct and anticipated future counter-cyclical payment rates are low compared to other crops. Even though these effects appear to be very small, current payment limitations may have limited expansion of farms specializing in upland cotton and rice production more than farms specializing in grain and oilseed production.

Table 4.6 Number of FSA farms categorized by the number of producers per farm

	1-2	3-5	6-10	11-20	21 or more	Total
Alabama	29,899	2,477	454	77	0	32,907
Alaska	70	2	0	0	0	72
Arizona	1,675	399	80	16	0	2,170
Arkansas	17,877	7,634	1,415	194	35	27,155
California	9,257	2,416	634	149	35	12,491
Colorado	14,151	3,330	347	35	4	17,867
Connecticut	1,528	52	7	0	0	1,587
Delaware	3,351	253	3	0	0	3,607
Florida	6,619	144	24	3	0	6,790
Georgia	35,815	1,979	176	8	0	37,978
Idaho	14,359	1,808	333	53	0	16,553
Illinois	132,526	24,416	1,571	153	18	158,684
Indiana	94,041	11,543	596	60	5	106,245
Iowa	138,779	10,724	544	42	5	150,094
Kansas	83,540	20,539	1,853	137	4	106,073
Kentucky	51,590	4,871	293	14	0	56,768
Louisiana	17,572	5,262	1,536	439	97	24,906
Maine	2,457	204	3	1	0	2,665
Maryland	11,136	809	12	0	0	11,957
Massachusetts	1,519	124	0	0	0	1,643
Michigan	51,686	3,632	173	23	1	55,515
Minnesota	92,483	5,067	246	8	1	97,805
Mississippi	24,010	3,781	945	179	32	28,947
Missouri	64,220	9,694	735	65	10	74,724
Montana	19,896	2,795	277	30	2	23,000
Nebraska	74,138	11,174	775	47	1	86,135
Nevada	372	35	0	0	0	407
New Hampshire	745	69	0	0	0	814
New Jersey	2,353	33	1	0	0	2,387
New Mexico	3,979	340	26	4	0	4,349
New York	22,271	1,554	59	0	0	23,884
North Carolina	50,261	3,571	361	32	3	54,228
North Dakota	50,589	5,333	458	35	17	56,432
Ohio	79,258	7,254	243	8	0	86,763
Oklahoma	47,691	5,153	451	39	0	53,334
Oregon	7,071	1,076	225	32	6	8,410
Pennsylvania	31,670	1,684	19	1	0	33,374
Rhode Island	142	0	0	0	0	142
South Carolina	20,771	761	210	2	0	21,744
South Dakota	44,640	5,051	349	13	0	50,053
Tennessee	35,916	4,927	455	15	0	41,313
Texas	86,837	19,213	2,453	287	37	108,827
Utah	3,642	212	19	2	0	3,875
Vermont	2,191	220	25	0	0	2,436
Virginia	29,334	1,060	63	0	0	30,457
Washington	7,745	2,878	658	80	12	11,373
West Virginia	3,727	74	3	0	0	3,804
Wisconsin	80,733	2,989	104	6	0	83,832
Wyoming	3,929	274	8	0	0	4,211
U.S. total	1,610,061	198,890	19,222	2,289	325	1,830,787

Source: USDA Farm Service Agency

Land Values, Rural Communities, Agribusiness Infrastructure, Planting Decisions, and Supply and Prices of Covered Commodities

Current farm programs certainly do affect land values, agribusiness infrastructure, planting decisions, and the supply and prices of covered commodities. In fact, there is strong evidence that a portion of government payments, which likely varies regionally, is bid into cash rents and capitalized into land values. Government payments support agribusiness infrastructure and affect the planting decisions and the supply and prices of covered commodities (see Chapter 5 for further discussion of the effects of government payments).

This chapter focuses more narrowly on the effects of current payment limits rather than on the effects of payments. The effects of current payment limitations on land values, rural communities, agribusiness infrastructure, planting decisions, and the supply and prices of commodities eligible for direct and counter-cyclical payments and marketing loan benefits are largely inconsequential. Few producers are affected by current payment limits and current limits only modestly reduce payments to producers.

Current payment limits reduce direct and counter-cyclical payments, which are decoupled from production, by about 1.6 percent. Producers can either elect to plant any crop, except in some instances fruits, vegetables, and wild rice, or not grow a crop and continue to receive direct and counter-cyclical payments so long as they comply with wetland provisions and conservation requirements, effectively control noxious weeds, and keep base acres in agricultural or conserving uses. Since direct and counter-cyclical payments for the most part do not depend on which crop is planted and few producers have payments reduced because of payment limits, current payment limits likely have essentially no effect on plantings and production of program crops.

Loan deficiency payments and marketing loan gains are paid on current production and a limitation on these benefits could affect supplies and prices of covered commodities. Currently, loan deficiency payments and marketing loan gains are limited to \$75,000 per person. This limitation does not affect the supplies and prices of covered commodities, since a producer reaching the payment limitation may capture the marketing loan benefit by either electing to forfeit the commodity held as collateral for a marketing assistance loan to the CCC or using commodity certificates to settle the loan.

Administrative Costs

In addition to the reduction in payments, current payment limitations impose other costs on producers. As indicated above, many producers who would otherwise be affected by payment limitations appear to partially or totally avoid current payment limitations by restruc-

turing their farming operations. Producers choosing to restructure may incur costs. These costs could include legal and other consulting fees and time spent to develop the necessary paperwork and to negotiate new crop share and cash rent agreements.

Producers must complete certain forms as required by the FSA to administer payment limitations. Producers must take time to fill out the forms needed to apply payment limits and to respond to inquiries if questions arise. The FSA estimated these costs for the Commission at about \$8 million annually (table 4.7). Producers' legal and consulting fees for forming entities to garner additional payments are not included in this estimate nor does the estimate include the cost of maintaining records and gathering information. Some producers may also seek legal advice and representation and incur additional costs if the farm business structure is challenged as a scheme or device to avoid payment limitations.

Current payment limitations reduce taxpayer costs by lowering payments slightly. These savings are partially offset by the government costs of implementing and enforcing payment limitation regulations. These costs include: employee and other expenses to oversee that forms related to the administration of payment limitations are filled out and filed properly; costs to load information electronically and to develop, maintain, and refine software used to track payments; and costs to investigate, gather evidence, and prosecute instances in which producers have either violated or appear to have violated regulations on payment limits. USDA spends about \$16 million a year on these activities. The estimate covers the cost of administering all payment limits relating to farm programs. The FSA was unable to isolate the costs of administering payment limits for the programs being considered by the Commission. The FSA county offices, which interact with producers and process forms used for payment eligibility and payment limitation determinations, incur the bulk of the government cost. USDA was unable to provide the Commission with an annual estimate of the payments recovered from those found to be in violation of payment limitation regulations.

Table 4.7. Annual government and producer costs of implementing farm program payment limits

Item	Dollars
FSA county offices ¹	12,063,188
FSA State offices ²	3,112,545
FSA Washington, D.C. staff ³	122,183
FSA cost for forms ⁴	28,157
USDA Office of the Inspector General ⁵	850,327
Total annual government cost	16,176,400
Producer cost for completing paperwork ⁶	7,883,952
Total annual government and producer cost	24,060,352

¹Source: FSA work measurement data. The estimate is an average for FY 1999 through FY 2002 and includes benefits and overhead.

²For this estimate, each FSA State office provided information on its FY 2002 expenses for implementing payment limitations.

³Cost of staff that writes regulations and handbooks and provides guidance to field staff.

⁴Source: FSA estimate submitted to the Office of Management and Budget in packet for approval of payment eligibility and payment limit forms. The estimate includes expenses for form development, printing, distribution, and storage.

⁵Source: Office of the Inspector General administrative data. The estimate is an average for FY 1999 through FY 2002 and includes the cost of audits and investigations primarily related to payment limitations. The estimate does not include the cost of audits and investigations that identified payment limitation issues incidental to the primary objectives or allegations.

⁶Source: FSA estimate submitted to the Office of Management and Budget in packet for approval of payment eligibility and payment limit forms. The estimate includes time needed to fill out forms and travel time. It is based on an average hourly wage of \$12.00.

Commodity Certificate Exchanges

The Joint Explanatory Statement of the Committee of Conference for the 2002 Act states, “The Managers intend for the Commission to examine the feasibility of improving the application and effectiveness of payment limitation requirements, including the use of commodity certificates and unlimited forfeiture of loan collateral.” Consequently, the Commission examined how certificates are used, how they are accounted for and tracked by USDA, and the general effects of their use.

Evolution of Certificates

The use of certificates in the operation of farm commodity programs became prominent in 1983 as a way to pay producers and dispose of government-owned inventory (Payment-in-Kind). Some farm program payments were paid in certificates rather than cash. The certificates were transferable and could be redeemed for surplus inventory. Redeeming certificates for government inventory became associated with the marketing assistance loan program when forfeitures of loan collateral became a concern in the late 1990s.

In the late 1990s, farm prices fell sharply as the world economy slowed, currencies of Asian countries and others depreciated sharply, and good weather resulted in large farm production. With prices well below loan rates, producers increasingly began to reach the \$75,000 payment limit on loan deficiency payments and marketing loan gains. As part of broad financial assistance to producers, Congress responded to the limitation on loan deficiency payments and marketing loan gains in two ways. In the Agriculture, Rural Development, Food and Drug Administration and Related Agencies Appropriations Act of 2000 (Public Law 106-78), enacted in October 1999, the per-person limit was increased from \$75,000 to \$150,000. In addition, the legislation amended the 1996 Act to provide the Secretary of Agriculture discretionary authority to make commodity certificates available to producers. The authority to issue commodity certificates was continued in the 2002 Act and the limit on loan deficiency payments and marketing loan gains was lowered to \$75,000 per person.

How Certificates Are Currently Used

Current law provides the Secretary of Agriculture discretionary authority to use four possible methods to make in-kind payments:

- delivery of the commodity at a warehouse or similar facility;
- transfer of negotiable warehouse receipts;
- issuance of negotiable certificates which the CCC exchanges for a commodity owned or controlled by the CCC in accordance with applicable regulations; or
- other methods deemed appropriate by the CCC to promote the efficient, equitable, and expeditious receipt of in-kind payments so that a person receiving the payments receives the same total return as if the payment had been made in cash.

In February 2000, the Secretary of Agriculture chose to implement commodity certificate provisions based on the third method listed above. For producers with outstanding nonrecourse loans, a three-step commodity certificate exchange mechanism was instituted to allow CCC to first acquire and then dispose of quantities of commodities pledged as loan collateral. The three-step process is outlined in the following table.

The certificate three-step process

Step	Action taken
1	Producer secures a marketing assistance loan from CCC, offering a specified quantity of a commodity as collateral, and receives the applicable loan rate for each unit of the commodity placed under loan.
2	Producer turns the loan collateral over to the CCC in full satisfaction of the loan and purchases a commodity certificate at the alternative repayment rate, which is the adjusted world price (AWP) or "CCC determined value," as applicable.
3	Producer exchanges the certificate for the quantity that was momentarily in CCC's possession.

The AWP is used for cotton and rice, and the CCC determined value is the Posted County Price (PCP) for other commodities. The AWP is the world market price adjusted to U.S. location and the PCP is the current U.S. terminal cash or spot market price adjusted for location. The certificate exchange process is not permitted if the AWP or the PCP is above the loan rate. The income gained from the use of certificates is essentially identical to that gained through a loan deficiency payment or marketing loan gain. After the certificate exchange, the producer's income is the receipts from the sale of the commodity at the market price plus the difference between the loan rate and the loan repayment rate—the AWP for cotton and rice and the PCP for other commodities.

The AWP is used as the alternative loan repayment rate for upland cotton and rice and the PCP is used as the alternative loan repayment rate for other crops eligible for marketing assistance loans. These two alternative loan repayment rates reflect the marketing assistance loan provisions contained in the 2002 Act. Under the 2002 Act, the Secretary is required to permit producers to repay marketing assistance loans for upland cotton and rice at a rate that is the lesser of loan rate or the world market price adjusted to United States quality and location (AWP). For other crops eligible for marketing assistance loans, the 2002 Act requires the Secretary to set the repayment rate at a rate that the Secretary determines will minimize potential loan forfeitures, minimize the accumulation of stocks, minimize the cost incurred in storing the commodity, and allow the commodity to be marketed freely and competitively in domestic and international markets. In response to this mandate, USDA has used the current cash or spot market price adjusted for location (PCP) to establish the loan repayment rate for all crops except upland cotton and rice.

Data on the Use of Certificates

Certificate use has grown sharply for two reasons. First, the lower market prices of the late 1990s and early 2000s caused an increase in producers reaching the \$75,000 (\$150,000 in some years) limit on loan deficiency payments and marketing loan gains. Cotton and rice prices were particularly low during the 2001 crop year. Second, certificates are used by Cooperative Marketing Associations (CMAs) and Loan Servicing Agents (LSAs) as a means to settle loans without having to track benefits received by each person in relation to payment limits. This reduces their administrative costs and allows CMAs to LSAs to freely market cotton and rice based on market conditions without considering whether a portion of the crop being marketed on behalf of their members is subject to payment limits (Bell).

If certificates were not available, the CMA or LSA would have to check with the FSA to determine if a member has reached the limit on loan deficiency payments and marketing loan gains. It may take the FSA several days to determine whether the producer's payment limit has been reached and to provide that information to the CMA or LSA. If a producer has reached the limit on payments, that producer's production would be ineligible for a loan deficiency payment or marketing loan gain. In order to avoid the additional administrative costs and additional marketing decisions involved when a producer reaches the limit on loan deficiency payments and marketing loan gains, many CMAs and LSAs have adopted the use of certificates as the preferred mechanism for obtaining marketing loan benefits for their members. As a result, not all certificate exchanges are a result of producers reaching the payment limit (GAO).

Table 4.8 shows the marketing assistance loan benefits derived from the use of certificates in recent years.

Another reason certificates and certificate exchanges are used is to encourage producers to settle marketing assistance loans when market prices are below loan rates rather than forfeit and deliver loan collateral to the CCC at loan maturity. Marketing assistance loans are a marketing tool for producers. Rather than market a commodity, a producer can choose to use current production as collateral for a nonrecourse loan. Access to the loan is not limited, giving all producers the option of forfeiting the collateral held for the nonrecourse loan to the CCC if market prices do not rise above the loan rate plus interest.

If, after harvesting a loan-eligible crop, market prices are below loan rates, a producer may obtain a loan deficiency payment on the crop and forgo the use of the loan program. Or, the producer may use the loan program and receive a marketing loan gain by placing the crop under loan and repaying the loan at some point during its life at the loan repayment rate. If

Table 4.8. Certificate exchange gains by crop year

	1999/00	2000/01	2001/02	2002/03F
	Billion dollars			
Certificate exchange gains	0.099	0.616	1.974	0.739
	Percent			
Gains as a share of total marketing loan benefits	1.2	8.2	24.1	40.8
Share of gains accounted for by cotton and rice	93.9	85.9	98.9	100

F = forecast.

certificates are not available, once a producer reaches the \$75,000 limit on loan deficiency payments and marketing loan gains, the producer could leave any remaining collateral under loan (or place additional production under loan, if eligible), and upon loan maturity, forfeit that collateral to the CCC. The producer would forfeit, because the gain realized by forfeiting the collateral to the CCC is not subject to the payment limit on loan deficiency payments and marketing loan gains.

Certificates help to prevent loan forfeitures. The gains realized by a producer from using certificates are also not subject to payment limits. This gives producers reaching the payment limit the additional option of purchasing certificates and using the certificates to purchase the loan collateral transferred to the CCC. The current \$75,000 limit applies to loan deficiency payments and marketing loan gains, while the certificate exchange is viewed as neither; it is a transfer of title of the producer's loan collateral to the CCC with the CCC then exchanging the commodity for a certificate that was sold to the producer at the market price.

Economic Effects of the Current Use of Certificates

The Commission examined the consequences of issuing certificates under current law to avoid forfeiture of commodities to the government. As an example of the costs and benefits of permitting the use of certificates, consider a cotton producer having a single payment limit (one person only) of \$75,000 on loan deficiency payments and marketing loan gains, who harvests 1,000 acres of cotton with a yield 800 pounds per acre. The loan rate is \$0.52 per pound and the adjusted world price (AWP) is assumed to be \$0.395 per pound, making the loan deficiency payment rate \$0.125 per pound. The market price is assumed to be \$0.42 per pound, as the domestic market price is usually somewhat above the AWP for cotton.

With no payment limit, assume this producer could elect at harvest to receive \$100,000 in loan deficiency payments (1,000 acres x 800 pounds per acre x \$0.125 = \$100,000). The producer would then be free to market the crop at any time. With the payment limit in effect, the producer would receive \$75,000 in loan deficiency payments on three-quarters of the cotton production and payments are reduced by \$25,000 (table 4.9). The producer could use the remaining one-quarter of production as collateral for a marketing assistance loan.

The crop used as collateral for a loan is assumed to remain under loan until loan maturity and then be forfeited to the CCC, if prices remain below the loan rate. Assuming the CCC disposes of the cotton immediately after forfeiture by selling it at the market price, the CCC would incur estimated storage charges of \$0.04 per pound (current law requires CCC to pay storage for cotton but not for other commodities eligible for marketing assistance loans) and interest to the Treasury is estimated at \$0.005 per pound. In addition, the CCC would incur the difference between the loan principal paid to the producer and the revenue from the sale of the cotton.

In this example, the producer is also worse off because the producer was unable to receive the difference between the domestic market price and the AWP on the crop that was put under loan and forfeited to the CCC. If the producer did not have the option of forfeiting the crop, the producer's income would decline by \$25,000 rather than by \$5,000 as indicated in the above table, assuming the entire crop was marketed at harvest.

Whether CCC costs decrease or increase depends on several factors, such as the relationship between the AWP and the domestic market price and the level of these prices during the marketing year. If the market price is below the loan rate at harvest and the market price does not increase after the crop is forfeited, the government can reduce farm program costs by issuing certificates to avoid forfeitures. However, if prices are expected to rise, the government may be able to reduce outlays by not issuing certificates and encouraging forfeiture. If the AWP is below the domestic market price, the income of the producer affected by the payment limit would decline if the government did not issue certificates.

Table 4.9. Effects of loan forfeiture on farm income and CCC costs (cotton example) ¹

Item	\$75,000 limit on LDPs and MLGs with certificates	\$75,000 limit on LDPs and MLGs without certificates that results in forfeiture		
		AWP - \$0.025	AWP + \$0.025	AWP + \$0.075
CCC resale price	N.A.	AWP - \$0.025	AWP + \$0.025	AWP + \$0.075
(1) LDP paid by CCC (12.5 cents/lb.)	\$100,000	\$75,000	\$75,000	\$75,000
(2) Storage cost	N.A.	\$8,000	\$8,000	\$8,000
(3) Interest	N.A.	\$1,000	\$1,000	\$1,000
(4) Net resale cost	N.A.	\$30,000	\$20,000	\$10,000
(5) Total cost to CCC (sum of 1-4)	\$100,000	\$114,000	\$104,000	\$94,000
(6) Loan principal	N.A.	\$104,000	\$104,000	\$104,000
(7) Producer cash receipts	\$336,000	\$252,000	\$252,000	\$252,000
(8) Producer gross income (1+6+7)	\$436,000	\$431,000	\$431,000	\$431,000

N.A. = Not applicable.

¹ Example: A producer with single payment limit harvests 1,000 acres of cotton yielding 800 pounds per acre; Adjusted World Price is 39.5 cents per pound; current market prices is 42 cents per pound; loan rate is 52 cents per pound.

Source: Commission estimates

Table 4.10. Effects of loan forfeiture on farm income and CCC costs (corn example) ¹

Item	\$75,000 limit on LDPs and MLGs with certificates	\$75,000 limit on LDPs and MLGs without certificates that results in forfeiture		
		PCP - \$0.10	PCP	PCP + \$0.10
CCC resale price	N.A.	PCP - \$0.10	PCP	PCP + \$0.10
(1) LDP paid by CCC (20.0 cents/bu.)	\$90,000	\$75,000	\$75,000	\$75,000
(2) Storage	N.A.	0	0	0
(3) Interest	N.A.	\$1,400	\$1,400	\$1,400
(4) Net resale cost	N.A.	\$22,500	\$15,000	\$7,500
(5) Total cost to CCC (sum of 1-4)	\$90,000	\$98,900	\$91,400	\$83,900
(6) Loan principal	N.A.	\$148,500	\$148,500	\$148,500
(7) Producer cash receipts	\$810,000	\$675,000	\$675,000	\$675,000
(8) Producer gross income (1+6+7)	\$900,000	\$898,500	\$898,500	\$898,500

N.A. = Not applicable.

¹ Example: A producer harvests 3,000 acres of corn; yield of 150 bushels per harvested acre; producer receives loan deficiency payments up to the payment limit; receives loan at \$1.98 per bushel; PCP \$1.78 per bushel; producer markets crop at \$1.80 per bushel.

Source: Commission estimates

While the above example applies to upland cotton, the results generally hold for other commodities (table 4.10). For other commodities, the CCC does not pay storage costs, reducing the cost to the CCC when the commodity is placed under loan. However, market prices must increase somewhat during the marketing year to cover interest costs incurred by the CCC and for total CCC costs under forfeiture to fall below the cost incurred by CCC when certificates are issued.

With certificates, the harvested crop would be marketed during the marketing year as determined by market conditions. If CCC does not issue certificates, the producer reaching the payment limit would likely keep the portion of the crop not eligible for loan deficiency payments or marketing loan gains under loan until maturity, at which time the loan collateral is forfeited. This interruption of usual marketing patterns could affect availability to users and market prices during the marketing year and could result in reduced international competitiveness and lost export sales. A partially offsetting market behavior is that when stocks are isolated from the market due to government programs, private stockholders may reduce their stocks. To the extent that this substitution occurs, the disruptive effects just described may be reduced.

Another potential market disruption of not using certificates is the timing of government sales. Most forfeitures are likely to occur late in the marketing year. Government sales at that time, or carried into the harvest period of the subsequent crop year, may weaken market prices at a time when prices are already low because of harvest-time pressure.

Conclusions

- The \$40,000 payment limit on direct payments in the 2002 Act is projected to reduce payments to producers by about 1.6 percent or \$85 million per year, assuming producers reaching the payment limit do not restructure further. The \$65,000 limit on counter-cyclical payments is also forecast to reduce payments by about 1.6 percent or \$125 million per year when market prices for all crops eligible for counter-cyclical payments are at or below their respective loan rates. About 1 percent of all producers are expected to have payments reduced because of current payment limits.
- A larger proportion of upland cotton and rice producers are affected by payment limits than producers of other crops eligible for direct and counter-cyclical payments. A higher percentage of upland cotton and rice producers reach the limit on direct and counter-cyclical payments, because direct and counter-cyclical payment rates per acre (payment rate times program yield) and average acreage per farm are generally higher for rice and upland cotton than for other crops eligible for direct and counter-cyclical payments.
- Many producers affected by payment limits are located outside of the traditional upland cotton and rice production areas. In 2001, producers in 43 States reached the limit on PFC payments. Furthermore, making soybeans, other oilseeds, and peanuts eligible for

direct and counter-cyclical payments under the 2002 Act will increase the number of producers that have payments reduced because of payment limits in the Corn Belt and in other regions that are important producers of these crops.

- Producers currently have many options available to them to organize their business operation, and farm organizational structure has greatly reduced the effectiveness of limits on direct and counter-cyclical payments. Nationally, 87.9 percent of farms had 1-2 producers (persons actively engaged), 10.9 percent had 3-5 producers, 1.1 percent had 6-10 producers, and 0.1 percent of farms had 11 or more producers in 2002. It appears likely that a number of the farms with a high number of producers may be structured for the primary purpose of lessening the reduction in payments that would otherwise result from payment limits.
- In 2002, there were 325 farms with 21 or more producers. Ninety percent of these farms were located in 9 States—Arkansas, California, Illinois, Louisiana, Mississippi, Missouri, North Dakota, Texas, and Washington. These States were among the leading States in terms of the reduction in payments and the number of producers that had payments reduced because of the 1996 Act's limit on PFC payments.
- Current payment limits have very little effect on land values, rural communities and agribusiness infrastructure, planting decisions, and supplies and prices of covered commodities. The limited effects reflect the fact that only a small percentage of producers of all covered commodities reach the current limits on direct and counter-cyclical payments; further, payments to those reaching the limits are reduced only modestly and many of the largest farms are structured to lessen the extent to which the limits reduce payments.
- Producers must complete certain forms as required by the FSA to administer payment limitations. The FSA estimates this cost to producers at about \$8 million annually. This estimate does not include producers' legal and consulting fees for restructuring the farming operation in response to payment limits or the cost of legal advice and representation, if the farm business structure is challenged as a scheme or device to avoid payment limitations.
- USDA spends about \$16 million a year to administer all regulations related to farm program payment eligibility and payment limits, including payment limit regulations that pertain to conservation and disaster programs. These costs include: employee and other expenses to oversee that forms related to the administration of payment limitations are filled out and filed properly; costs to load information electronically and to develop, maintain, and refine software used to track payments; and costs to investigate, gather evidence, and prosecute instances in which producers have either violated or appear to have violated regulations on payment limits.
- Producers can avoid the current limit on loan deficiency payments and marketing loan gains by forfeiting nonrecourse marketing assistance loans or using commodity certificates. The use of commodity certificates avoids loan forfeitures, which are not currently subject to payment limits.

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- The use of certificates under current marketing loan provisions results in little expected savings or costs to the taxpayer and only a slight increase in income for producers who would otherwise reach the payment limit and forfeit crops held as collateral for marketing assistance loans. Certificate exchanges arguably avoid potential market disruption both during the marketing season, as stocks that would otherwise be held under loan are free to be marketed, and at the end of the season, when the government would otherwise likely sell forfeited loan stocks.

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