

# Integrated Farm Revenue Program

## How It Works and Why It's More Effective

### Effective and Efficient

To ensure a safe and secure food supply, farmers need a safety net when disaster hits and tools to help them manage risk. But existing commodity programs are complex and costly for taxpayers, not applied equitably—and they often fail to provide protection when needed.

American Farmland Trust (AFT) proposes a new safety net, one that will benefit conservation by enhancing the long-term viability and competitiveness of American agriculture. The new safety net is based on revenue protection that will:

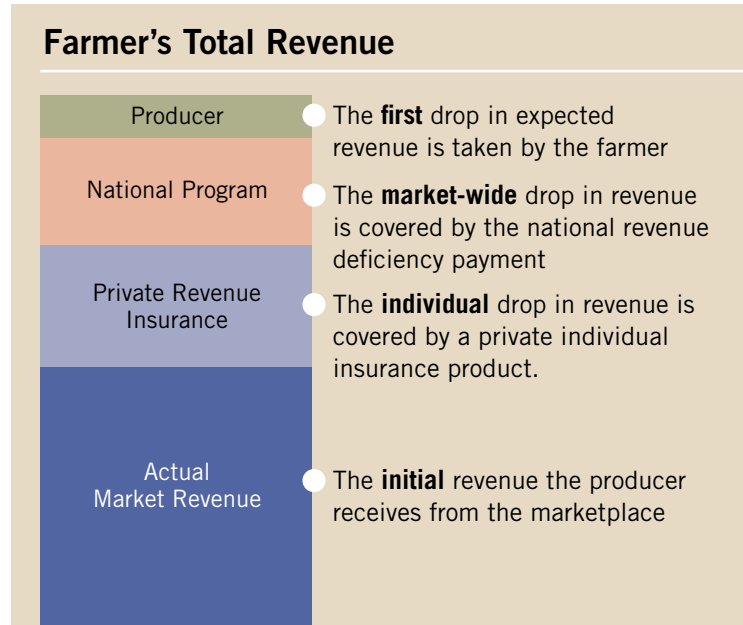
- Provide better protection by targeting revenue rather than price;
- Replace existing counter-cyclical (CCPs) and loan-deficiency payments (LDPs) with more comprehensive, cost effective risk management tools;
- Be market-oriented, less trade distorting and more equitable;
- Help the environment by reducing incentives to produce on marginal land; and
- Integrate safety net programs to enable private revenue insurance to function more effectively.

### Integrated Revenue Protection—How It Works

Producers, the government and the private sector each have a role in managing risk. AFT's revenue protection proposal, developed by agricultural economist Dr. Carl Zulauf of Ohio State University, is based on the premise that farmers face two types of risk: at the national market level, such as widespread drought and drops in prices: and second, at the individual farmer level, such as localized frost.

These different risks require a two-tier, but integrated farm revenue program that brings crop insurance—currently operating separately from commodity payments—into the farm bill.

With an integrated program, farmers rely on private insurance at the individual level, while the government handles risk management for widespread national losses where the private market is ineffective. By replacing counter-cyclical and loan-deficiency payments and integrating crop insurance, payments will be less erratic and more effective at covering risk. This program allows for planting decisions to be based on market signals rather than politically set targets. It is easily administered within the existing FSA structure and is already familiar to current participants. Additionally, all program crops would be treated equally.



## Tier 1: National Revenue Deficiency Program

A national revenue deficiency program supported by the federal government protects farmers from uninsurable, nationwide risks such as a sudden price drop or a widespread drought, while still encouraging farmers to plant based on market signals.

### National Revenue Deficiency Program Example: Soybeans 2004

1. At the beginning of each growing season, a national projected per acre revenue is calculated by multiplying the forecasted national average price by the expected national average per acre yield.
2. After harvest, a national per acre realized revenue is calculated based on actual prices received and actual nationwide average yields.
3. Deficiency payments are based on the difference between projected revenue and the actual revenue.
4. A deficiency payment percentage is applied to each farmer's production history ensuring payments are proportional.

Projected U.S. Yield (February):	39.3 bu/acre
December Futures Price (February):	x \$6.72/bu

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**Projected U.S. Revenue: = \$264/acre**

Realized U.S. Yield (October):	41.4 bu/acre
Harvest Insurance Price (October):	x \$5.26/bu

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**Realized U.S. Revenue: = \$218/acre**

Projected	\$264/acre
– Realized	– \$218/acre

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**Revenue Deficiency Payment: = \$46/acre**

**National average payment applied to individual farms: *17% payment***

The National Revenue Deficiency Program therefore provides per acre payments based on unexpected drops in national revenue during the growing season. While the current system sends false price signals to producers, this proposed program would reset the national projected revenue each year, thus reducing market distortions, overproduction and production on marginal lands.

## Better Protection and Lower Costs

Farmers need risk management tools. This proposal provides farmers with tools to make decisions based on actual market conditions instead of “planting for the program.” The current separation of programs—commodity payments and crop insurance—causes inconsistent payments and higher expenses for taxpayers. The current programs also leave large gaps in coverage because they do not distinguish between market and individual risk.

### Better Protection

Existing commodity programs are narrowly focused on supporting prices, not revenue. For example, in 2002, typical corn farmers in Mercer County, Ohio, and in many parts of the Midwest, suffered from yields that were about half the size of the previous year's yields due to a drought. As a result, farmers saw their average revenue drop to \$161 per acre, down from an expected \$350 per acre. However, because average prices for corn were high that season, farmers did not receive assistance from current safety net programs. This is one example of many that have occurred during the life of the 2002 Farm Bill. Under AFT's integrated farm revenue program,

## Tier 2: Individual Revenue Insurance Program

Private insurance protects a farmer's individual revenue loss due to localized events such as flooding or drought.

The individual revenue insurance program would operate much like it does currently. However, it would only cover a farmer's individual revenue loss if it were greater than the national loss. This integration is the key to better functioning risk management tools, and it provides significant cost savings.

### Integrated Individual Revenue Insurance Example: Soybeans 2004

1. Farmer chooses a level of protection (e.g., 75% coverage) to insure a certain level of guaranteed revenue.
2. After harvest, the farmer's actual revenue is calculated.
3. A farmer's loss is the difference between individual guarantee and realized revenue.
4. Any national deficiency payment made to the farmer is subtracted from the farmer's loss and the farmer is paid the difference.

Farmer's Expected Revenue	\$264/acre
Farmer's Insurance Coverage Level	x 75%
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<b>Individual Guarantee:</b>	<b>= \$198/acre</b>
Farmer's Realized Yield:	26 bu
Harvest Insurance Price:	x \$5.26/bu
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<b>Farmer's Realized Revenue:</b>	<b>= \$137/acre</b>
<b>Farmer's Loss</b>	<b>\$61</b>
- National Deficiency Payment	- \$46
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<b>Insurance Indemnity Payment:</b>	<b>\$15/acre</b>
AFT's proposal is similar to Crop Revenue Coverage (CRC) and Revenue Assurance (RA)	

#### *Better Protection and Lower Costs continued*

farmers would get protection when they need it—when they experience a drop in revenue—and would reduce the economic justification for the almost yearly disaster payments that have cost \$1.8 billion annually.

#### **Lower Costs**

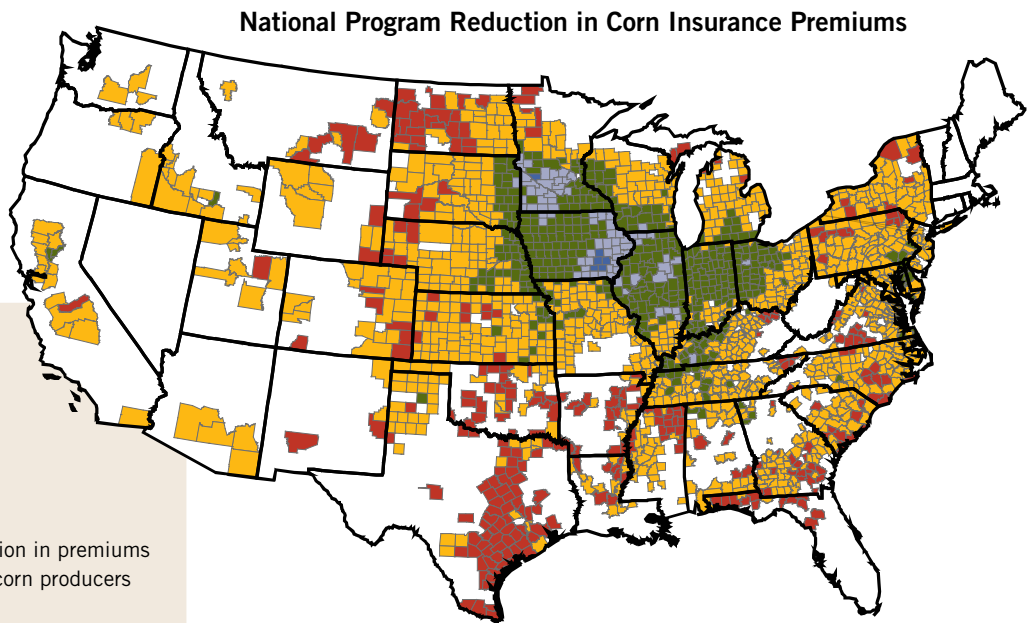
An integrated farm revenue program would reduce excessive government payments. For example, in 2005, the same Mercer County, Ohio farmers, and many others throughout the country, experienced a very different situation that resulted in unnecessary payments. In that year, prices were low but yields were up so revenue was fine. However, because existing programs are triggered only by low prices regardless of yields, farmers received payments on average of \$99 per acre—payments that were not really needed during a good revenue year. In contrast, AFT's approach would have avoided excessive payments by focusing on farmers' loss in revenue.



## Impact on Insurance

With the government removing the systemic or market-wide risk, private insurance can provide individual revenue insurance at higher coverage levels to protect against losses that exceed the national average.

Farmers also will be able to secure higher levels of coverage at equal or lower cost. The map below illustrates that corn producers would see on average a 46 percent reduction in insurance premiums at the 75 percent coverage level when compared with the current revenue assurance contract. Soy producers are expected to receive a 29 percent reduction in premiums and wheat producers can expect a 22 percent reduction.



These reductions would allow producers across the country to purchase a more efficient insurance product at better rates than currently exist. Through integration, producers receive better insurance products, taxpayers use money more wisely and crop insurance becomes a more central element in the farm safety net.

## What's the Bottom Line?

Compared to the current farm bill risk management programs—commodity payments and crop insurance—AFT's Integrated Farm Revenue Program would cost approximately the same amount. However, it's a more responsible use of taxpayer dollars because it provides better protection for commodity farmers, is more market oriented, and eliminates the need for emergency disaster payments to commodity producers.

For more information about this or any of the policies recommended in *Agenda 2007*, please visit AFT's Web site at [www.farmland.org](http://www.farmland.org) or send an email to [info@farmland.org](mailto:info@farmland.org).