

Insurance Is An Effective Within-Year Price Safety Net But Fails Across Years



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In early October, Senator Richard Lugar of Indiana, author of the Conservation Reserve Program (CRP) in 1985 and Chair of the "Senate Agriculture, Nutrition, and Forestry Committee in 1966" when Freedom to Farm was adopted, announced the introduction of a farm bill proposal that would save "\$40 billion in USDA Cuts to Help Meet Federal Deficit Reduction Goals." The bill was co-sponsored by Rep. Marlin Stutzman, also of Indiana.

According to a Lugar Press release: "The Rural Economic Farm and Ranch Sustainability and Hunger Act (REFRESH) would reform farm programs, cutting \$16 billion, a 24.5 percent reduction. Conservation programs would be updated and streamlined for a savings of \$11.3 billion, a 17.6 percent reduction. Nutrition program eligibility loopholes would be closed saving \$13.9 billion, only a 2 percent reduction. Roughly two-thirds of the savings would come from farm and conservation programs, and a third from nutrition programs, which represent three-fourths of the USDA budget."

In introducing the bill, Lugar said, "This bill provides good farm and nutrition policy and saves \$40 billion. Farm Bill politics has long frustrated reform efforts by myself and others. The current urgency to meet our deficit reduction targets gives us the chance to make smart changes. We offer our bill as a thoughtful option for consideration by the House and Senate Agriculture Committees, as well as the Congressional Deficit Reduction 'Super' Committee charged with making real federal spending cuts by the end of the year."

As announced, "The Lugar-Stutzman bill would end current farm programs including direct payments to farmers, counter-cyclical payments, the ACRE program and marketing assistance/loan deficiency payments. The REFRESH bill would establish an aggregate risk and revenue management (ARRM) program that allows producers to protect between 90 percent and 75 percent of their expected crop revenue. All farmers would be able to purchase supplemental revenue insurance that is underwritten by the USDA Risk Management Agency."

The proposed legislation would also repeal the present no-net-cost sugar program and replace the present dairy programs with a "a voluntary margin protection program that covers 80 percent of the producers' production history when

margins fall below \$4 per hundred-weight."

In addition, the Lugar-Stutzman legislation would reduce CRP acreage from the current level of 29 million enrolled acres to 24 million enrolled acres. Additional conservation savings would come from "combining and improving efficiencies in Wetland Reserve Program, the Grasslands Reserve Program, the Farm and Ranch Lands Protection Program, and the Healthy Forest Reserve Program. Similar consolidations and efficiencies would be found in the Environmental Quality Incentives Program (EQIP), Conservation Stewardship Program, the Agricultural Water Enhancement Program, and the Wildlife Habitat Incentive Program (WHIP)."

Lugar-Stutzman expects to generate \$14 billion in savings in the Nutrition title through closing loopholes, eliminating government overlap, and improving the efficiency of the Supplemental Nutrition Assistance Program (SNAP)—formerly known as Food Stamps.

In some of its features, the Lugar-Stutzman bill is similar to other 2012 Farm Bill proposals in eliminating direct payments, counter-cyclical payments, and marketing assistance/loan deficiency payments. The Farm Bureau proposal also targeted what the authors see as inefficiencies in SNAP.

According to Gary Schnitkey of the University of Illinois crop insurance, like the insurance that is the basis of the Lugar-Stutzman proposal "provides coverage for events that causes revenues to decline within year.... Crop insurance will not provide protection against price declines that occur across years that typically persist across multiple years."

What that means is that one of the assumptions that Lugar and Stutzman had to make in their proposal is that, on average, crop prices are just about right – they cover the cost or production and allow for a reasonable profit. For this to happen supply and demand need to remain relatively balanced.

If growth in supply exceeds demand growth for a multiple-year period, then the Stutzman-Lugar bill will run into the same problem as the 1996 Farm Bill that Lugar presided over. Prices will plunge and the level of insurance offered based on price expectations at planting time will plunge. Price expectation thus may remain well below the cost-of-production for years at a time. The Lugar-Stutzman legislation provides an excellent price safety net when prices are high and there is no need for a price safety net, while providing an ineffective price safety net when prices are well below the cost of production as they were in the 1998-2001 period – the phrase "Emergency Payments" comes to mind.

One can assume that there will never be a repeat of the situation of the 1998-2001 period, but we remain unconvinced. △

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