

FINANCE NUCLEAR WASTE PROGRAMS WITH SURCHARGE  
ON NUCLEAR POWER GENERATION  
(A-270-c)

Savings from CBO Baseline	Annual Savings (millions of dollars)					Cumulative Five-Year Savings
	1983	1984	1985	1986	1987	
Budget Authority	225	250	275	300	325	1,375
Outlays	225	250	275	300	325	1,375

Nuclear power plants produce highly radioactive spent nuclear fuel that can be reprocessed to capture reusable uranium. Until recently, reprocessing was prohibited in this country as part of a national policy to discourage the proliferation of nuclear materials. With the future use of reprocessing still uncertain, the spent fuel must be disposed of as waste. In 1982, the government will spend about \$200 million on research to determine the best means and places to dispose of the spent fuel. The Congress is now considering legislation that would lead to the construction of repositories. It is estimated, however, that repositories will not be ready until nearly 2000.

Since consumers of nuclear-generated electricity primarily benefit from the nuclear waste program, it might be appropriate for these consumers, rather than all taxpayers, to pay for current research and development (R&D) and future construction of disposal facilities. A surcharge of about one-half mill per kilowatt hour on nuclear-generated electricity would raise enough funds for continued R&D activities through the early 1990s. This would increase the average consumer's electricity price by less than 1 percent, while providing additional receipts of about \$1.4 billion during the 1983-1987 period. If the Congress authorizes construction of disposal facilities, the increased spending levels would require a higher fee.

Such a surcharge would recover the costs of the nuclear waste programs from the beneficiaries and might improve efficiency in utility companies' decisionmaking. It would, however, raise prices for consumers and contribute to inflation. The timing and degree to which the surcharges were passed on to consumers would vary, depending on the form of the surcharge and its treatment by individual state public utility commissions.

PRICE URANIUM ENRICHMENT AT FAIR-MARKET VALUE  
(A-270-d)

Savings from CBO Baseline	Annual Savings (millions of dollars)					Cumulative Five-Year Savings
	1983	1984	1985	1986	1987	
Budget Authority	12	0	98	131	175	416
Outlays	525	600	660	665	700	3,150

In order to function, the light water reactors generally used in U.S. nuclear power plants require more U-235 than is found in natural uranium. The process that increases the U-235 content is called uranium enrichment. The U.S. government provides this enrichment service for all domestic and some foreign utilities, accounting for about 72 percent of free-world enrichment activities in 1980.

Currently, the government does not charge as much for the enrichment service as private firms would. The government is permitted by law to recover only its historic costs, whereas private businesses routinely cover the costs of taxes, insurance, and a return on equity in their charges. The Department of Energy (DOE) estimates that this cost recovery policy has provided a cumulative subsidy of \$5.5 billion (in 1979 dollars) to the nuclear industry over the 1954-1980 period.

The federal government usually does not charge the equivalent of private-sector prices for its services, because most of them are provided in areas in which private firms could not operate. In uranium enrichment, this is not the case. The government retains its monopoly for national security reasons rather than because private firms could not profitably perform the enrichment services. Thus, fair-market pricing for uranium enrichment warrants consideration. Imposing a fair-market price for enrichment services could increase costs to the purchasing utilities by roughly 31 percent during 1983-1987, generating additional revenues (or outlays savings) of \$3.2 billion.

Proponents contend that such a pricing shift would promote efficiency and reduce the uranium enrichment program budget. These savings are also contingent, however, upon the pricing policy of DOE's competitors. Recently, its major European competitor, Eurodif (a consortium including France, Italy, Belgium, and Spain), dropped its price significantly to compete with the anticipated 1982 DOE price. The estimated savings assumes that, if the Congress enacted a fair-value price, Eurodif would raise its price to about the same level. Critics of fair-value pricing contend that this would not happen and that such a policy would undermine DOE's competitiveness in the long run as European competition continued to price below cost. Opponents also argue that this could encourage the proliferation of nuclear weapons as the United States loses its dominance in providing enrichment services.

In the short term, the United States might want to retain its market share of enrichment services by maintaining its present pricing policy. Over the long term, if European competitors persevered in price-cutting below costs, the U.S. government might question the wisdom of providing these enrichment services.

CUT SUBSIDIES FOR SYNTHETIC FUELS  
(A-270-e)

Savings from CBO Baseline	Annual Savings (millions of dollars)					Cumulative Five-Year Savings
	1983	1984	1985	1986	1987	
Budget Authority	0	0	0	0	0	0
Outlays	34	36	37	39	40	186

Synthetic fuels, which are substitutes for oil and gas products, are produced by processing plentiful resources such as coal and oil shale. The Synthetic Fuels Corporation (SFC), an independent federal entity, was created in 1980 to assist the private sector to develop a number of commercial-sized synthetic fuel plants. The SFC, with \$12.2 billion in budget authority granted before 1983, functions primarily as an investment bank. It is authorized to provide loan guarantees, price guarantees, purchase agreements, and direct loans. In exceptional circumstances, the SFC may participate in joint ventures with private firms.

If the Congress decided to abolish the SFC, the potential outlay savings would probably amount to only \$186 million during 1983-1987. Because it concentrates on financial arrangements that require little or no outlays unless projects fail, the short-term outlays should be relatively low, although the government would remain exposed to potential high costs. Since synfuel projects require a number of years to build, large budget outlays caused by project failure or default are not likely to occur until after 1987. The exact impact cannot be calculated, since there is no basis on which to predict how the SFC will allocate financial assistance among the available options and what the failure and default rates might be.

The purpose of the additional production from SFC-assisted synthetic fuel plants is to make the U.S. economy less vulnerable to potential interruptions of imported oil and to assist the U.S. transition to alternative fuels to offset declining domestic oil and gas reserves. The SFC was first suggested during a period when domestic oil prices were controlled at below market value. Controlled crude oil prices limited the market's ability to give correct signals about the potential competitiveness of synthetic

fuels, thus reducing the incentives for developers to proceed. With the recent decontrol of oil prices and the scheduled deregulation of natural gas prices by 1985, market forces rather than government regulation will probably determine investment decisions about commercial development of synthetic fuels. Under these circumstances, the SFC might no longer be needed.

On the other hand, since the SFC fosters synthetic fuel development, it might provide some additional insurance against the effects of a future interruption in foreign oil supplies. SFC proponents contend that such insurance outweighs the possible inefficiencies that might result from SFC subsidies. They also argue that the United States will have to make the transition to synthetic fuels eventually, and therefore, the experience provided by early plants will be helpful in choosing the appropriate technologies.

REDUCE REA INTEREST SUBSIDIES AND  
 TARGET REA LENDING MORE EFFICIENTLY  
 (A-270-f)

Savings from CBO Baseline	Annual Savings (millions of dollars)					Cumulative Five-Year Savings
	1983	1984	1985	1986	1987	
Budget Authority (Off-budget)	300	700	1,400	2,000	2,600	7,000
Outlays (Off-budget)	300	700	1,400	2,000	2,600	7,000

The Rural Electrification Administration (REA) was created to spur development of electric and telephone service in rural areas. This goal has been fulfilled--99 percent of the nation's farms now have access to electricity and 95 percent to telephones. The REA, however, continues to support the financing activities of utility cooperatives located primarily in rural areas, lowering their costs of building new generating plants and transmission and distribution networks. In areas that have changed from rural to urban, utilities are still eligible for REA assistance, as are rural utilities that charge electric rates below the national average.

The REA provides loans to rural electric and telephone cooperatives through a heavily subsidized direct loan program and a loan guarantee program that is essentially a direct loan program funded through the Federal Financing Bank (FFB). Direct REA loans are made at 2 or 5 percent interest for terms of up to 35 years, while REA-guaranteed FFB direct loans are made at a rate marginally higher than the long-term Treasury borrowing rate and for terms of up to 35 years.

For 1982, the Congress has specified that REA make minimum commitments of \$1.1 billion in direct loans and \$5.1 billion in guaranteed loans. These levels will bring cumulative commitments for REA direct loans to \$16.9 billion and for loan guarantees to \$31 billion by the end of 1982. Over the next five years, the FFB is expected to fund over \$25 billion in REA-guaranteed loans. This amount is almost as large as the total on-budget expenditures for energy activities. It is twice the amount authorized for the

Synthetic Fuels Corporation, and also exceeds federal spending for the Strategic Petroleum Reserve.

Possible ways to reduce the substantial federal off-budget outlays for REA activities include increasing the interest charged on direct loans and reducing annual guaranteed loan commitments to one-half the level that would be provided under current Congressional allocations. These two proposals would decrease federal off-budget outlays by about \$7 billion over the 1983-1987 period.

The argument for increasing interest rates on direct loans centers on the cost of providing credit at rates significantly less than the government itself must pay and the fact that the relative subsidy provided by these interest rates has grown significantly since it was first enacted. At present interest rates, every \$100 million in direct REA loans will cost the government about \$215 million over the life of the loans. Increasing interest charges to three percentage points below Treasury borrowing costs would reduce federal costs by over \$300 million between 1983 and 1987, while still providing borrowers with access to credit at rates substantially less than private market rates, under favorable loan terms, and with significant savings in lending costs.

A reduction in the loan guarantee level would be aimed at ensuring that limited credit resources were allocated to the most effective and essential uses. Virtually all of the REA guarantees apply to loans for electric transmission and generation facilities. No other energy function receives such unrestricted access to federal financing. The ranges imposed by the Congress are set to accommodate the upper limits of the cooperatives' projections of their power supply needs. The REA guarantees are not contingent upon the types of planning and efficiency criteria required of other federal power projects, most notably those included in the 1980 Pacific Northwest Power Planning and Conservation Act (PNPPCA).

While the credit market would function most efficiently if the cooperatives were required to use private-sector financing in lieu of federal guarantees, equity and national goals for power and telephone capacity may support the retention of some federal assistance. As an alternative to an abrupt termination of the REA loan guarantee program, lending could be focused on projects meeting efficiency criteria, and loan guarantees reduced to a level that would serve only those projects that most clearly support national goals. For example, a 50 percent reduction in guarantee

commitments would reduce off-budget outlays by \$6.7 billion over the next five years.

Several options are available to achieve greater efficiency in the REA loan guarantee program and thus limit the adverse effects of funding reductions. One approach would be to reduce the demand for federal lending by increasing the interest rate charged by the FFB for the guaranteed loans. Another option would be to use a more competitive selection process in extending guarantees. Competition could be based on planning, conservation, and management standards similar to those required for the Bonneville Power Administration under the PNPPCA. Alternatively, the REA guarantee program could be modeled after the approach taken in the Energy Security Act. Eligibility criteria also could be tightened according to the types of borrowers or facilities.

A decrease in the interest subsidy for REA direct loans is likely to increase electricity and telephone costs to consumers served by cooperatives. The magnitude of this increase will depend on the government's long-term borrowing rate and on the debt structure of the cooperatives. Decreasing loan guarantee levels might increase the price and limit the availability of electric and phone service, because cooperatives would be more dependent on private-sector financing for meeting future load growth.

INCREASE PRICE OF BUREAU OF RECLAMATION IRRIGATION WATER  
(A-300-a)

Savings from CBO Baseline	Annual Savings (millions of dollars)					Cumulative Five-Year Savings
	1983	1984	1985	1986	1987	
Budget Authority	22	47	73	101	132	375
Outlays	22	47	73	101	132	375

The Reclamation Act of 1902 established the Bureau of Reclamation to administer development of arid and semiarid lands in 17 western states. Most of the bureau's projects have been designed primarily to provide water for agricultural irrigation. Of the 30.1 million acre-feet of water delivered to users by the bureau in 1979, 93 percent was sold for irrigation. Instead of setting user fees for irrigation water on its cost, the government bases fees on the users' ability to pay and/or on a percentage of original construction costs without interest. In 18 major projects, the bureau sells water at an average price of \$9.34 per acre-foot, while the average cost for these deliveries is about \$58.00 per acre-foot.

If the price of this water was gradually raised until users paid the full cost, receipts would increase by \$132 million in 1987. For example, in the lower Yellowstone project, the bureau now sells water at \$5.28 per acre-foot. The estimated full cost of this water is \$34.62 per acre-foot, and energy industries in the region would pay from \$200 to \$500 per acre-foot for the same water.

Proponents of full-cost pricing contend that the subsidy promotes inefficiency, indirectly causing water scarcities. According to the General Accounting Office, the government's full costs of delivering water often exceed the added income that irrigation brings farmers. Opponents assert that western agriculture has developed because of subsidized water prices and that full pricing would require a major adjustment by users; thus any policy to cancel the subsidy should be phased in slowly to let farmers convert to less water-intensive methods. Others contend that, because the subsidy's benefits are widespread, they are in the public interest.

ALLOCATE FEDERAL GRAZING RIGHTS AT MARKET RATES  
(A-300-b)

Savings from CBO Baseline	Annual Savings (millions of dollars)					Cumulative Five-Year Savings
	1983	1984	1985	1986	1987	
Budget Authority	3	9	17	25	33	87
Outlays	3	9	17	25	33	87

Several federal agencies allow grazing on land under their jurisdictions. Two of these--the Department of Defense (DoD) and the Bureau of Indian Affairs (BIA)--receive market values for the grazing rights by auctioning them. The agencies with the largest land-holdings--the Forest Service and the Bureau of Land Management (BLM)--allocate grazing rights by permit, and are required by law to collect fees based on beef cattle prices, forage values, and other costs associated with raising cattle. These grazing fees have not been as high as nearby commercial rates or bids made for comparable grazing on DoD or BIA land.

The Forest Service and BLM collected about \$38 million in 1981 in grazing fees, at the rate of \$2.30 per animal unit per month (AUM). (Comparable private rates vary from \$5 per AUM to \$12 per AUM.) If new legislation required these grazing rights to be auctioned by sealed bid (with the required minimum designated at the currently legislated fee) rather than allocated by permit, the average fees could more than double, and the annual revenue gain would be about \$33 million in 1987. This assumes that, by 1987, 80 percent of all permits would be auctioned and half of those auctioned would be sold at rates approximating those on DoD and BIA land. The other half are assumed to sell at rates just above the current regulated price.

Proponents claim that market rates established by auctioning grazing permits would not only pay for a larger part of the costs of public range management, but would also give better signals to federal officials of the relative values of land parcels under their management. Furthermore, some believe that much western land is overgrazed because the permit costs are relatively low. Market rates would balance use of land with the land's capability to provide food.

Defenders of the current arrangements assert that permit fees represent fair value, considering the deteriorated condition of much public land from overgrazing. Further, the present holders of grazing permits have arranged their business affairs in the belief that current practices will be continued. Opponents of this change contend that the disruption caused by auctioning permits would be unfair to these holders.

CHANGE FEDERAL-STATE SHARE OF MINERAL RECEIPTS  
(A-300-c)

Savings from CBO Baseline	Annual Savings (millions of dollars)					Cumulative Five-Year Savings
	1983	1984	1985	1986	1987	
Budget Authority	146	159	175	192	207	879
Outlays	146	159	175	192	207	879

Federal gross receipts from bonuses, royalties, and rentals resulting from development of onshore mineral resources on public domain lands totaled approximately \$750 million in 1981 and may increase considerably in future years. These receipts are shared with the states containing the public lands, with 90 percent for Alaska (except 50 percent from the National Petroleum Reserve) and 50 percent for all other states. Before the law was changed in 1976, the share for states other than Alaska was 37.5 percent.

The Congress could increase net federal receipts by about \$900 million over the 1983-1987 period by reducing the share for all states to the former 37.5 percent. The major reason for such a proposal is that the federal government bears substantially more of the costs of producing the resource than do state governments. 1/

States oppose this change principally because of the costs to them of rapid energy development. Because energy development on federal land often occurs near nonfederal land, some costs spill over to adjacent areas and are borne by state and local governments. In addition, state and local governments may have cash flow problems because they may experience significant preproduction expenses but do not receive payments until the resource is produced.

1. It is also true that the current net federal share is most likely less than 50 percent because of revenue losses resulting from the tax deductibility of resource payments. Because the marginal rates of those making payments are much higher for federal than for state taxes, the federal share of net receipts, after tax effects are considered, is much lower than the state share. Reducing the state share of gross receipts to 37.5 percent would produce about a 50-50 split of net receipts.

INCREASE ENTRY CHARGES FOR OUTDOOR RECREATION AREAS  
(A-300-d)

Savings from CBO Baseline	Annual Savings (millions of dollars)					Cumulative Five-Year Savings
	1983	1984	1985	1986	1987	
Budget Authority	30	60	94	97	100	381
Outlays	30	60	94	97	100	381

Federal recreational areas have more than 800 million visitors each year. In 1980, fewer than 5 percent of these visitors paid entrance fees, producing net revenues of only \$5 million (after collection costs were deducted), compared with annual costs of about \$350 million simply to maintain the visited areas. On the average, visitors who paid fees in 1980, paid less than 20 cents per person to enter federal recreational facilities. If the Congress increased these entry fees to an average of 60 cents per person (after collection costs) and required the responsible agencies to collect fees from 20 percent of all visitors, net receipts would increase by about \$100 million in 1987.

It is impractical to collect entry fees at many federally owned natural areas; in some remote areas, collection costs would exceed receipts. At most dams or water impoundments and the traditional national parks, however, entry fees are feasible and cost-effective. Similar facilities managed by states or municipalities routinely charge entry fees in order to recover costs of services. The park system in Canada is financed in large part through entry fees.

Opponents of proposals to increase or extend park entry charges make several points. They argue that a major purpose of the national parks is preservation of a unique resource for future generations, and that the cost of this should be borne by all taxpayers. They also assert that a price cannot and should not be put on the value of access to the Grand Canyon and similar national treasures. On the other hand, the recreational agencies are spending about \$350 million per year to maintain recreational facilities for visitors. Increasing entry fees would defray a part of these costs.

REDUCE FUNDING FOR EPA CONSTRUCTION GRANTS  
(A-300-e)

Savings from CBO Baseline	Annual Savings (millions of dollars)					Cumulative Five-Year Savings
	1983	1984	1985	1986	1987	
Budget Authority	200	200	1,040	1,095	1,155	3,690
Outlays	0	20	70	230	500	820

Municipalities have received federal grants to construct wastewater treatment plants under various authorizations since 1957. The Federal Water Pollution Control Act Amendments of 1972 considerably expanded this program by requiring the Environmental Protection Agency (EPA) to provide 75 percent of the allowable construction costs for approved projects. The Clean Water Act of 1977 authorized EPA to fund 85 percent of projects using alternative or innovative technologies. In recent years, outlays have been around \$4 billion annually.

In 1981, the Congress significantly modified the program. The 1982 authorization level was lowered from \$5.0 billion to \$2.4 billion, with \$2.6 billion authorized annually for 1983 through 1985. Of this \$2.6 billion, \$200 million was reserved annually for combined sewer overflows into marine bays and estuaries.

In 1985, three other program changes will be implemented. First, only 20 percent of a state's allotment can be spent on major rehabilitation of sewers, new collector sewers, and combined sewer overflow. Second, projects must be designed only for current population needs, rather than for anticipated future growth. Finally, the federal share of the construction costs will be reduced from 75 to 55 percent.

To obtain additional savings, the Congress could make further program changes. Large savings would result from further reducing the federal share of construction costs--for example, from 55 percent to 45 percent--with corresponding reductions in budget authority, and by eliminating entirely the funds for major rehabilitation of sewers, new collector sewers, and combined sewer overflow. (Under current law, beginning in 1985 governors would be allowed to

use up to 20 percent of a state's allotment for these otherwise ineligible projects.) These two changes could be implemented by decreasing budget authority 35 percent annually beginning in 1985. Budget authority could be cut by another \$200 million annually, beginning in 1983, if the authorization for combined sewer overflow into marine bays and estuaries was eliminated. Removing the current two-year time limit on obligation of funds would save smaller amounts. Together, these proposals would reduce budget authority and outlays by \$3.69 billion and \$820 million, respectively, over the 1983-1987 period.

These changes could improve the program's efficiency in several ways and thereby partially offset their effect on water quality. First, larger state or local contributions to capital costs would reduce the potential incentive to build overly expensive and sophisticated treatment plants. Second, eliminating funds for several categories of projects would concentrate resources on those that contribute most to improving water quality. Third, removing the time limit on obligation of funds could eliminate the possibility that many projects funded at the end of the obligational period are those "ready-to-go," rather than those of higher priority, but not yet ready for funding.

Critics of these changes present several arguments. The recently enacted cut in the federal share from 75 to 55 percent (effective in 1985) may adequately discourage municipalities from building overly sophisticated plants, and perhaps some experience should be gained with the 55 percent share before further reducing it. Although major rehabilitation of sewers, new collector sewers, and combined sewer overflow may generally be less deserving of funding than treatment projects, this may not be true in every case. It might be better to leave some discretion to the states. Further cuts in the federal share and elimination of eligibility for certain projects would increase the financial burden on state and local governments beyond those likely to result from recently enacted program changes. Funding level decreases of the magnitudes suggested here would leave most states with annual allotments of \$20 million or less, which is very modest compared with an average project cost of \$15 million. Finally, the current two-year time limit on obligation of funds results in the reallocation of unobligated funds to other states. By eliminating the time limit, money would be allocated solely by an allotment formula that might not correspond to the most efficient distribution of funds.

ELIMINATE FmHA FARM LOAN INTEREST SUBSIDIES  
(A-350-a)

Savings from CBO Baseline	Annual Savings (millions of dollars)					Cumulative Five-Year Savings
	1983	1984	1985	1986	1987	
Budget Authority	0	51	94	115	127	387
Outlays	0	51	94	115	127	387

The Farmers Home Administration (FmHA) makes farm ownership and operating loans at subsidized interest rates to limited-resource farmers. Limited-resource farmers are identified by FmHA as: (1) beginning farmers having adequate training or farm experience but lacking sufficient resources to enter farming; (2) farmers adjusting their operations by buying farmland or changing enterprises, and farmers requiring loans to remain in business; and (3) disadvantaged farmers with serious deficiencies in resources, income, credit, education, and living standards. Currently, limited-resource borrowers are charged 11.5 percent for farm operating loans and 7 percent for farm ownership loans, as compared with 14.5 and 13.25 percent charged to regular borrowers. Since the limited-resource loan program was begun in fiscal year 1979, FmHA has loaned about \$1.5 billion to nearly 32,000 limited-resource farmers. Current law requires that at least 25 percent of FmHA's farm loans go to such borrowers. In addition, FmHA makes emergency disaster loans to farmers unable to obtain credit elsewhere; these loans carry an interest rate of 8 percent--about half of FmHA's cost of obtaining the funds it is lending. Eliminating interest subsidies on both the limited-resource farm loans and the emergency disaster loans would save a total of about \$387 million over 1983-1987.

The principal objective of the limited-resource loan program is to assist low-income farmers to increase their production, income, and living standards. While there may be other reasons for public financing of limited-resource farmers, this activity does not result in any measurable increase in production. Thus, interest subsidies could be eliminated without detriment to the nation's long-term food and fiber production capacity.

Clearly, there are high entry and expansion costs in farming. The elimination of FmHA interest subsidies would mean that some persons would have to leave farming and others who want to become farmers would not be able to do so. On the other hand, there is much uncertainty about the potential for limited-resource borrowers to become financially independent of FmHA.

FmHA also makes emergency disaster loans to farmers at highly subsidized interest rates when applicants are unable to obtain credit elsewhere. If a farmer is in fact creditworthy, there is no policy reason to charge less than FmHA's own borrowing costs; and if he is not creditworthy, the case for making any loan at all is weak. Further, the availability of such subsidized disaster aid discourages participation in the federal crop insurance program, which charges a premium to participants.

REDUCE THE LEVEL OF DAIRY PRICE SUPPORT  
(A-350-b)

Savings from CBO Baseline	Annual Savings (millions of dollars)					Cumulative Five-Year Savings
	1983	1984	1985	1986	1987	
Budget Authority	0	0	900	1,300	1,600	3,800
Outlays	900	1,300	1,600	1,600	1,600	7,000

The federal government supports the price of milk by purchasing manufactured dairy products. The current support price is \$13.10 per hundredweight of milk. Under the Agriculture and Food Act of 1981, the minimum level of milk price support must rise to \$13.25 on October 1, 1982, to \$14.00 a year later, and to \$14.60 on October 1, 1984. For 1983, 1984, and 1985, these price support levels are about 68, 67, and 65 percent of parity, respectively.<sup>1/</sup> Under certain conditions, the minimum level of support rises to 70 or 75 percent of parity.

The dairy price support program has increased farm milk prices at the expense of consumers and taxpayers, but it has also helped to stabilize the dairy industry, resulting in an assured supply of milk and dairy products. In the past two years, however, milk price supports have been at a level that has contributed to a sharp expansion in milk production. In fiscal year 1981, the commercial supply of milk exceeded commercial use by about 10 percent, with all the excess purchased by the federal government at a cost of almost \$2 billion.

There appears to be small prospect of commercial milk supply coming in line with consumption by 1986, because the 1981 legislation continues to give dairy farmers the signal to increase production. Thus, federal dairy price support outlays are projected to remain relatively high under current policy.

1. Parity is the price, in current dollars, that gives milk the same purchasing power per unit in terms of goods and services bought by farmers as prevailed in the base period, January 1910 to December 1914.

The costs of this program will not decline unless milk production more nearly matches the demand for milk. One option would be to bring about a total 15 percent reduction in the current level of support in four six-month intervals beginning April 1, 1982--a decline from \$13.10 per hundredweight of milk to \$11.10 per hundredweight beginning in fiscal year 1984.

Such an approach would provide an orderly adjustment process with a predictable decline rather than a predictable increase in support levels. As compared with current policy, it would cause annual average farm prices of milk to be about 15 percent lower during 1983-1985, and annual milk production to average about 5 percent less. Lower farm prices would reduce average consumer prices for milk and dairy products by about 8 percent compared with current policy. Consumption, therefore, would average about 1 percent more per year. Because of reduced production and increased consumption, government purchases would decline, resulting in savings of \$0.9 billion in 1983 and about \$7 billion over the 1983-1987 period.

This option would cause dairy farmers to experience a real loss of income. During 1983-1985, dairy farmers' annual cash receipts would average about 20 percent less than under current policy. Such a sharp decline would likely cause some farmers to leave the industry. It might also lead to more volatile prices, since milk supply and demand would be in close balance by 1986; there is evidence that milk supplies and prices are more volatile when government purchases are less than 2 percent of annual milk production. To reduce the risk of an unstable dairy sector and higher prices to consumers, it might be necessary to increase the level of price support slightly after three years.

ELIMINATE FARM DEFICIENCY PAYMENTS  
(A-350-c)

Savings from CBO Baseline	Annual Savings (millions of dollars)					Cumulative Five-Year Savings
	1983	1984	1985	1986	1987	
Budget Authority	0	0	250	0	0	250
Outlays	250	0	0	0	0	250

NOTE: CBO projects no deficiency payments over 1984-1987, but under a less favorable farm price scenario annual payments could reach \$4 billion.

In the mid-1960s, U.S. policy began to shift away from high domestic price supports and rigid supply controls, allowing domestic grain and upland cotton prices to adjust gradually to world price levels. Payments were made to assist farmers in this adjustment. From the mid-1960s to the early 1970s, income payments--which averaged \$3 billion annually--were an important part of crop farmers' incomes. In the mid-1970s, deficiency payments--based on differences between target prices and market prices--were authorized for wheat, feed grains, upland cotton, and rice as a replacement for payments not tied directly to market prices.

In crop years 1974 through 1980, a total of about \$2.5 billion of deficiency payments was made. About \$1 billion of deficiency payments were made in crop year 1981 as a result of higher target prices, low crop prices, and because more farmers participated in the programs. Deficiency payments are highly concentrated among larger farmers and are of small economic consequence to most.

The Food and Agriculture Act of 1981 continues deficiency payments for the 1982-1985 crops. While CBO's baseline projection shows no deficiency payments for most of that period, a fall in farm prices could trigger payments of up to \$4 billion annually.

Given the evolution of agricultural policy, deficiency payments have largely fulfilled their function and could now be eliminated without detriment to domestic agriculture. Other provisions