AGRICULTURAL PRICE SUPPORT PROGRAMS
A LAYMAN'S GUIDE

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PREFACE

This guide, which was prepared at the request of the House Budget Committee staff, describes the fundamentals of existing farm programs. It was prepared by Robert M. Gordon of CBO's Natural Resources and Commerce Division under the direction of Douglas M. Costle and Kenneth L. Deavers. Helpful comments were provided by Victor Senechal, Rudie Slaughter, James Vermeer, James Vertrees, Mindy Upp, and Lynn Daft.

For more than four decades, the federal government has used a variety of techniques to support farm prices and stabilize the income of farmers. Programs administered by the Agricultural Stabilization and Conservation Service (ASCS) of the Department of Agriculture currently provide floor prices for wheat, corn, barley, soybeans, cotton, peanuts, tobacco, rice, milk, wool, and several other agricultural products. This document describes the various devices used to support agricultural prices and summarizes major features of existing commodity programs. In keeping with CBO's legislative mandate, this paper contains no recommendations.

I. METHODS USED TO SUPPORT FARM PRICES

The Department of Agriculture now relies on five methods to support commodity prices and stabilize farmer incomes: (1) production controls, (2) nonrecourse loans, (3) payments, (4) purchases of commodities, and (5) marketing orders. For most crops, production controls are reinforced by a payment, loan, or purchase program. The multiple combinations reflect the many laws and amendments that have accumulated since the early 1930s.[1] The principal methods of support are examined in more detail below.

(1) Production Controls

Agricultural production can be controlled by limiting the amount of acreage planted in crops. The tools now available for use, singly or in combination, are acreage allotments, cropland set-asides, and marketing quotas.

Acreage Allotments. Each year before planting time, the Department estimates the quantity of a particular commodity that will be needed to satisfy both domestic needs and export requirements. This quantity is converted into acreage and then apportioned among states, counties, and farms. The individual farmer's share is called an acreage allotment. If allotments alone are in effect, farmers can utilize more than the specified acreage without suffering financial penalties on the "excess" production, though they usually lose their eligibility for price support loans (discussed below).

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1 Current programs are authorized by the Agricultural Adjustment Act of 1938, the Commodity Credit Corporation Charter Act, the Agricultural Act of 1949, the National Wool Act of 1954, the Agricultural Act of 1970, the Agriculture and Consumer Protection Act of 1973, and the Rice Production Act of 1975.

Cropland Set-asides. The Agriculture and Consumer Protection Act of 1973 authorizes the use of cropland set-asides for upland cotton,[2] wheat, and feed grains (corn, grain sorghum, and barley). The Rice Production Act of 1975 authorizes set-asides for rice. If the Department forecasts excessive supplies of any one of these crops in the coming crop year,[3] a set-aside program is put into effect. Farmers who wish to be eligible for price support loans, payments, and purchases must set aside a specified portion of their land and use it for designated conservation purposes. The diverted acreage must be land that is as productive as the rest of the farm and land that would be planted in the absence of controls. The remaining acreage can be used for any crop except those governed by marketing quotas (see below).

If the Secretary of Agriculture finds that greater restrictions are necessary, he can ask for diversions beyond the set-aside requirement. Farmers who make these additional adjustments are entitled to compensation. In 1974 and 1975, set-asides were not used because supplies were not excessive and the department wanted to encourage production.

Marketing Quotas. Marketing quotas, which are used in combination with acreage allotments, limit the marketing of certain commodities by imposing financial penalties on any production in excess of the quota. The crop grown on the allotment acreage is the farm's assigned quota.

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2 Of the two major types of cotton grown in the U.S., upland and extra-long staple, upland is the most important, accounting for over 99 percent of total U.S. cotton production in recent years.

3 Crop years for different commodities begin on different dates. For fieldcrops, the crop year generally begins at time of harvest. The beginning of the crop year for major commodities is as follows: January 1-wool; April 1-dairy; June 1-oats, barley, rye, and flaxseed; July 1-wheat and flue-cured tobacco; August 1-rice, peanuts, and cotton; September 1-soybeans; and October 1-corn, grain sorghum, and burley tobacco.

Marketing quotas are currently in effect for extra-long staple (ELS) cotton, peanuts, and most kinds of tobacco. The Secretary is required by law to propose quotas for tobacco whenever production exceeds domestic needs and export requirements. 4 In the case of ELS cotton and peanuts, however, quotas must be proclaimed every year, regardless of supply conditions. Quotas had also been used for wheat and upland cotton, but these were suspended by legislation initially enacted in the 1960's and later by the 1973 act for the 1974-77 crop years.

After proclamation, quotas go into effect only if approved by two-thirds of the producers voting in a national referendum. If ratified, all producers who are not granted exemptions are penalized for any production from acreage in excess of that assigned under their allotment. The penalties often involve an excise imposed at some percentage of parity.5 In addition, producers may forfeit eligibility for price support loans or may face reductions in future marketing quotas and levels of price support.

(2) Nonrecourse Loans

Nonrecourse loans provide a guaranteed floor under the farm price of several commodities. This level of support is either specified in the authorizing legislation or set by the Secretary in accordance with guidelines established by Congress.6

Before every planting season, the Secretary announces the loan level for each commodity. If farmers find that market

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4 In the case of tobacco, a poundage quota is established for each farm. The quotas are proclaimed when output exceeds normal supplies by 5 percent and are proposed for three years after the initial proclamation.

5 The parity price is the rate that will give a unit of a farm commodity the same purchasing power, or exchange value in terms of goods and services bought by farmers, as farm commodities had in the base period 1910-1914.

6 In the case of some feed grains, the Secretary has considerable discretion. The loan rate need only be "fair and reasonable" in relation to that established for corn. For many crops, however, the Secretary must use a specified formula or set the loan rate at a percentage of the "parity price."

prices are low after harvest, or if they simply need working cash, they can put their crops in storage and use them as collateral for a loan from the Commodity Credit Corporation (CCC). These loans are usually made directly to eligible farmers or cooperatives through county offices of the Agricultural Stabilization and Conservation Service (ASCS) and are normally available to producers for 8 to 10 months following the harvest. The basis for eligibility varies from one commodity to another. The amount loaned is equal to the volume placed in storage times the established loan rate. At any time before the date of maturity, usually 12 months after the loan is made, the farmer can repay the loan (plus accrued interest) and redeem his crop. Alternatively, if market conditions remain unfavorable, the producer can keep the loan. In this case, the farmer forfeits his commodity to the government and the loan is satisfied. Most of the government's commodity stocks are acquired in this manner.

(3) Payments

Support payments take three forms: "deficiency" payments for the crops covered by the Agriculture Act of 1973 and the Rice Production Act of 1975; compensatory payments for losses caused by natural disasters; and supplementary payments used to raise producer returns to the support level.

Deficiency Payments. The Agriculture Act of 1973 established a new support mechanism for wheat, feed grains, and upland cotton known as the deficiency payment. The Rice Production Act of 1975 adopted the same mechanism for rice. Under these laws, participating farmers are provided two forms of price protection for their crops: "target prices" and the nonrecourse loans discussed above. The target prices are set above the loan rate and were adjusted in 1976 as they will be again in 1977 to reflect changes in production costs and productivity. If the U.S. average market price for the first five months of the crop year (calendar year for cotton) falls below the target price, producers of that crop become eligible for a deficiency payment. The payment is equal to the difference between the target price and the higher of the loan rate or the average market price, times the expected normal production of the acreage allotment. Only farmers who participate in the set-aside program (if in effect) are eligible for deficiency payments.

The deficiency payments are based on national yield data adjusted for differences in the productivity of individual farms. Total payments are limited to $20,000 per farmer from all the crop programs combined. Excluded from the limitation are loans, purchases, and compensation for land diversions beyond the set-aside requirement.

Disaster Payments. The 1973 and 1975 acts also provide a form of crop insurance for upland cotton, wheat, feed grains, and rice. A farmer becomes eligible for federal disaster payments if some natural disaster either prevents planting or causes the harvest on his allotted acreage to be less than two-thirds of the normal yield. Payments for the deficiency are at least one-third of the target price. In fiscal year 1975, the Department spent $556 million on disaster payments.

Supplementary Payments. Payments are made to producers of ELS cotton, wool, and mohair to raise their returns to the support level. Direct payments are used in combination with nonrecourse loans to maintain the support level for ELS cotton. Wool and mohair are supported entirely by payments. Producers of these commodities receive a payment equal to the difference between the support price and the average market price.

(4) Direct Purchases

Producers of honey and dairy products are guaranteed a floor price through a purchase mechanism. Products that cannot be sold on the open market at the established support level will be purchased at that price by the CCC. In the case of milk, the government buys the less perishable "manufactured milk products," i.e., cheese, powdered milk, and butter.

(5) Federal Marketing Orders

Federal marketing orders are agreements between producers and the Department of Agriculture that either fix the wholesale price of farm products or support prices indirectly by controlling the supply of commodities reaching the consumer. Orders are now in effect for milk and a variety of fruits and vegetables. The major features of marketing orders are discussed more fully in the descriptions of the individual commodity programs.

II. PRICE SUPPORT PROGRAMS FOR MAJOR COMMODITIES

Wheat, Upland Cotton, and Feed Grains

Prices of wheat, upland cotton, and feed grains are supported by a combination of deficiency payments, nonrecourse loans, and cropland set-asides. Participation is voluntary, but, as indicated above, only those producers complying with the set-aside program are eligible for payments or loans. Support for barley is left to the discretion of the Secretary. Disaster payments are also made available to eligible producers.

A national acreage allotment representing the acreage required to produce enough of the three crops for domestic needs and export is established every year. Each farm is assigned a share of this national allotment. The farm allotment does not restrict the level of production but is used only as a base for the calculation of deficiency payments. If it becomes necessary to make loans, however, they are provided for the farmer's total production, not just that harvested from allotment acreage.

Target prices for the 1974 and 1975 crop years for wheat, corn and upland cotton are specified in the 1973 act and have been adjusted in 1976 and will be again in 1977 for changes in productivity and production costs. Target prices for grain sorghum and barley, which are set by the Secretary, are pegged to the target price of corn. The loan levels for wheat and corn must fall within a specified range — a minimum level cited in the 1973 act and a maximum that is related to parity prices. Loans for the other feed grains are based on the loan level selected for corn. The loan rate for upland cotton is based on the price of American cotton in world markets. Target prices and loan rates for the 1975 and 1976 crops appear in Table 1. The figures show that market prices in early 1976 were substantially above prevailing target prices.

Table 1

SUPPORT PRICES FOR CROP YEARS 1975 AMD 1976 AND RECENT MARKET PRICES FOR MAJOR COMMODITIES
($/bushel unless otherwise indicated)

Commodity	Target Price 1975 Crop	Target Price 1976 Crop	Loan Price 1975 Crop	Loan Price 1976 Crop	March 15, 1976 Price Received by Farmers
Wheat	$2.05	$2.29	$1.37	$1.50	$3.65
Corn	1.38	1.57	1.10	1.25	2.50
Grain Sorghum	2.34/cwt	2.66/cwt	1.88/cwt	2.13/cwt	4.09/cwt
Barley	1.13	1.28	.90	1.02	2.34
Upland Cotton	.38/lb.	.432/lb.	.3427/lb.	.3712/lb.	.504/lb.
Soybeans	n.a.	n.a.	n.a.	2.50	4.46
Peanuts	n.a.	n.a.	.197/lb.	a	.187/lb.[b]
Rice	n.a.	8.00/cwt	8.06/cwt	6.00/cwt	5.86/cwt
Flue-cured Tobacco	n.a.	n.a.	.932/lb.	1.06/lb.[c]	1.00/lb.[d]
Burley Tobacco	n.a.	n.a.	.961/lb.	1.092/lb.[c]	1.056/lb.[d]

n.a. Not applicable
a. Not yet announced.
b. December 15, 1975 price.
c. Estimate
d. Average auction price, crop year 1975.

Sources: Market prices: Crop Reporting Board, Statistical Reporting Service, Agricultural Prices, March, 1976. Target prices and loan rates: U.S. Department of Agriculture news release, February 24, 1976.

Soybeans

Under provisions of the Agricultural Act of 1949 the Secretary of Agriculture is authorized to make available price support loans for several commodities, including soybeans. The level of support can be set up to 90 percent of parity. Though no loan program was in effect for soybeans in 1975, it has been reinstated for the 1976 crop year. The 1976 loan rate will be $2.50 per bushel, well below the March 1976 farm price of $4.46 per bushel.

Peanuts

Peanut prices are supported by marketing quotas and by nonrecourse loans provided through the three peanut grower associations. The Secretary is required by law to propose a marketing quota every year, regardless of supply. If two-thirds of all peanut producers endorse the quota in a referendum — as they have for the past 30 years — the loan level can be set at some point between 75 and 90 percent of parity. The specific level is determined by supply conditions. If producers rejected the quota, the support level would drop to 50 percent of parity. When a marketing quota is in effect, penalties are applied to the excess production of growers who do not comply with their acreage allotments. The national average support level for 1975 was $.197 per pound. The average price received by farmers during December, 1975, was below this level — about $.187 per pound.

Rice

The Rice Production Act of 1975 suspends marketing quotas and penalties for the 1976 and 1977 rice crops and replaces them with a system of deficiency payments, nonrecourse loans, disaster payments, and set-asides, similar to those in effect for wheat, upland cotton, and feed grains. Though there are no restrictions on production, only rice produced from allotted acreage will be eligible for loans and payments. And only those producers or farms having an allotment in 1975 receive allotments under this act. The national allotment for the 1976 and 1977 crops is legislatively set at 1.8 million acres.

Should the prospective rice carryover exceed 15 percent of total supply for the crop year, the Secretary of Agriculture is authorized to require participants in the program to set aside acreage. The Department has announced that there are no set-aside requirements for the 1976 crop.

A target price of $8.00 per cwt and a price support of $6.00 per cwt is specified in the legislation, both of which are to be adjusted by changes in the cost of production and changes in yield in 1976 and 1977. The average price received by farmers on March 15, 1976 was $5.86 per cwt. Payments under the rice program are limited to $55,000 per person per year.

Extra-Long Staple Cotton

The price of ELS cotton is supported through use of a combination of nonrecourse loans and supplementary payments. As with peanuts, marketing quotas for ELS cotton must be proposed every year, regardless of the supply situation. If the quota is approved by producers, the loan rate can be set between 50 percent and 100 percent above the loan level established for upland cotton. In addition, if the quota is approved, supplementary payments are made available at a rate which, together with the loan level, brings the support price to 65 to 90 percent of the parity price for ELS cotton. The acreage eligible for payment is determined by a factor related to the 1966 national acreage allotment. As with other commodities, if quotas are disapproved, the support level is reduced to 50 percent of parity and no payments are available. In recent years, the quotas have been endorsed by about 90 percent of the producers.

The national average loan level for the 1975 crop was 67.74 cents per pound, or twice the loan level for upland cotton. This is the statutory maximum. The 1975 payment rate was 6.36 cents per pound which raised the total support level to 74.10 cents per pound, equivalent to 65 percent of parity. Farm prices during January 1976 averaged 81 cents per pound.

Tobacco

For program purposes, tobacco is divided into three types: burley, flue-cured, and a category that includes Puerto Rican, sun-cured, and cigar tobaccos. The prices of all three classes are supported through use of marketing quotas and loans made to growers through their marketing associations.

Marketing quotas for flue-cured tobacco are expressed both in terms of acreage and poundage; any production in excess of 110 percent of the poundage ceiling is subject to penalties. Excessive output is ineligible for loans and is deducted from the quota for the following year. If production falls below the quota, the difference will be added to the ceiling for the next crop. Only poundage quotas are applied to the burley crop. Production exceeding 110 percent of the quota is subject to the same penalties applied to the flue-cured crop. Quotas for most varieties are proposed when production exceeds the "normal" supply by five percent and if approved, remain in effect for three years. Marketing quotas are now applied to most types of tobacco.

Loan rates are also established for each grade of tobacco. The support level is determined by adjusting the 1959 support price upward or downward according to changes in the index of prices paid by farmers (Parity Index)[7] for the three preceeding calendar years.

Dairy Products

Prices of fluid milk and other dairy products are supported through direct purchases and marketing orders. The purchase program is administered by the ASCS and financed through the CCC.

The Agriculture Act of 1949 requires a support price to be adjusted annually to between 75 and 90 percent of parity. In 1975, the level of support was set at 80 percent of parity, which yielded a support price of $7.24 per hundredweight. The Department has announced plans to set the support level at 80 percent of parity again for the 1976 marketing year which begins April 1, 1976. This price applies only to "manufacturing milk," i.e., the grade of milk used for cheese, butter, and powdered milk, though, in effect, it determines the price of fluid milk as well. If producers are unable to sell their milk at this support level, the CCC will purchase carlots of manufactured products at announced prices and remove them from the market to raise the U.S. average price to the support level. In addition, the CCC may also buy manufactured products in consumer-size packages through competitive bids. The prices normally equal the announced price for bulk milk plus processing and packaging costs.

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[7] The "Parity Index" is a measure of changes in the average prices paid by farmers for goods and services used in family living and in production.

Dairy products purchased by the CCC are used for domestic and international food assistance. If government stocks are insufficient for these programs, the CCC may also buy dairy products at prevailing market prices.

In most parts of the country, the prices paid to farmers by processors are fixed by federal milk marketing orders. The 61 orders now in effect govern the pricing of about 60 percent of all U.S. milk sold to plants and dealers.[8]

The marketing order program allows the producers in each marketing region to fix wholesale prices through a "classified" pricing system. Manufacturing grade milk is designated Class II and is given a price based on the national support level. Drinking grade, or Class I milk, is priced higher to reflect the more stringent sanitary standards and additional processing costs. If the prices are approved by the Agricultural Marketing Service, the Secretary issues an "order" to enforce the pricing system throughout the marketing region. Producers receive a "blend" price, or weighted average of the two prices.

Fruits and Vegetables

Federal marketing orders for a variety of fruits and vegetables influence prices indirectly by controlling the supply reaching the consumer. Three general types of programs are now used for fruits and vegetables: grade, size, and quality standards; rate of flow regulations; and volume controls.

By enforcing grade and size standards, marketing orders can be used to reduce the quantity marketed and thereby support prices. Rate-of-flow controls even out the flow of produce to the market, helping to avert periodic gluts and shortages and attendant fluctuations in prices. These programs have been used primarily for citrus products. Quantity controls are used to divert excess supplies away from primary markets into alternative outlets such as noncompeting food uses or nonfood uses. They are used to regulate the marketing of storable crops such as dried fruits and nuts and rely on market allocations or reserve pooling arrangements.

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[8] Most states and metropolitan areas are covered by federal orders. Several states operate their own programs for intrastate commerce, which resemble the federal system.

Wool and Mohair

The National Wool Act of 1954 and sections of the Agriculture Act of 1973 provide that support of wool and mohair prices be carried out through payments to producers. The 1973 act extended the 1971 support levels through 1977. Wool is currently supported at 72 cents per pound and mohair at 80.2 cents per pound.

The payments made in any year are determined by the differential between the average price received by all producers during the preceding marketing year and the support level. In April of every year, the Department calculates the average return received by the producers during the preceding year. If that figure falls short of the support level, the difference is converted into a percentage which is used to raise the average return up to the support price. Each producer's payment is then determined by applying the percentage factor to his own proceeds from the sale of wool or mohair. For example, the average price received by wool producers during the 1974 marketing year was 59.1 cents per pound. The multiplication factor required to raise the average return up to the support level of 72 cents was therefore (72/59.1) or 1.22. Although the payment for the 1975 crop has not been announced yet, it is expected to be about $60 per $100 of wool sales. Support payments are not provided if the average sales price exceeds the support level.[9]

It should be noted that under this program, producers are not guaranteed the support price. Those who receive less than the average price for their product will receive less than the support level. Similarly, the producer who received a higher than average market price for his wool also gets a higher support payment. This method of payment was designed to encourage producers to improve the quality and marketing of their wool.

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9 Prices received by mohair producers in 1975 were in the range of $2.50 to $3.00 per pound, well above the support level of 80.2 cents per pound. Hence, no payments will be made for mohair.

Table 2

PRICE SUPPORT METHODS USED FOR MAJOR COMMODITIES

Crop	Acreage Allotment	Cropland Set-Aside	Marketing Quota	Deficiency Payment	Disaster Payment	Supple-mentary Payment	Non-Recourse Loans	Direct Purchases	Federal Marketing Orders
Wheat	X	X		X	X		X		
Corn	X	X		X	X		X		
Grain Sorghum	X	X		X	X		X		
Barley	X	X		X	X		X		
Upland Cotton	X	X		X	X		X		
ELS Cotton	X		X			X	X		
Peanuts	X		X				X		
Rice	X	X		X	X		X		
Tobacco	X		X				X		
Milk/Dairy Products								X	X
Fruits/Vegetables									X
Wool/Mohair						X			
Soybeans							X		