How Does the USDA Farm Bill Proposal Measure Up?

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On January 31, US Agriculture Secretary Mike Johanns announced a proposed revision of the current Farm Bill, which could result in a decrease of the most trade-distorting forms of domestic support.

Overall, the proposal would spend an estimated US$10 billion less over the next 10 years than projected spending for the 2002 Farm Bill, which is set to expire in September 2007. Much of the anticipated savings are from expected high prices for many commodities in future years. However, the Johanns proposal actually would spend US$5 billion more from 2008 – 2012 than simply extending the existing provisions in the 2002 Farm Bill.

Most of the proposed changes tend to move Farm Bill programmes towards more market-oriented supports and away from the most trade-distorting (Amber Box) forms of subsidies.

Under the 2002 Farm Bill, most commodity subsidies are distributed under three main programmes:

- loan deficiency payments. These subsidies are paid when farm prices fall below specified levels. Loan deficiency payments are based on current production, and are generally understood to be trade-distorting. They are defined as Amber Box under WTO rules.
- counter-cyclical payments. Subsidies paid when prices fall below specified levels. These payments are based on historical rather than current production. Under current WTO rules they are considered trade-distorting and would likely be classified as Amber Box subsidies. In the Doha Round agriculture negotiations, the US has proposed new criteria that would allow counter-cyclical payments to qualify as Blue Box subsidies.
- direct payments. Subsidies based on historical acreage and yields, meant to be 'decoupled' from production and therefore less trade-distorting. Direct payments are intended to be classified as Green Box subsidies.

What Would Change?

The Johanns proposal makes changes to each of these programmes.

Loan deficiency payments: The trigger prices for subsidies would be lowered, resulting in reduced subsidies, since payments are only made if market prices fall below the trigger prices. In addition, if market prices remained consistently below the trigger price, the trigger price itself would be lowered to 85 percent of the five-year Olympic average of market prices. This will tend to reduce subsidies over time, even if prices are low. With current high price projections, payments for this programme are expected to be minimal, if not nothing at all in comparison to historical payments in the billions.

In addition, the Johanns proposal would reform the way farmers can claim payments under this programme, making it more difficult to play games and reducing errors that result in payments when prices are not low.

Loan Rates: The 2002 Farm Bill vs the Johanns Proposal

Loan Rates	Wheat	Corn	Soybeans	Rice	Cotton
2002 Loan Rate	US$2.80	US$1.95	US$5.00	US$6.50	US$0.52
New Loan rate	US$2.94	US$1.93	US$4.96	US$6.53	US$0.39
Percent Change	5.04%	-1.02%	-0.83%	0.39%	-24.26%

Counter-cyclical payments: The Johanns proposal would make significant changes to counter-cyclical payments. The main innovation would be to transform the programmes from compensating for low prices to compensating for low revenues. Farmers complain that the current counter-cyclical payments only help in times of low prices, but not in the event of poor production. The Johanns revenue-based counter-cyclical payment takes both yield and price into the equation.

The new revenue-based counter-cyclical programme would operate at a national level on a commodity-by-commodity basis. Payments would be triggered when the actual national revenue is less than the target national revenue for an individual commodity. In this instance, all participating farmers for each commodity would receive a payment based on 85 percent of their historical acreage, yield and the payment per acre. Based on Oxfam calculations and high price forecasts, only cotton will receive payments under this programme, averaging US$1.2 billion per year, which is roughly equal to those under the price-based programme.

Direct Payments: The Johanns proposal would boost direct payments. For most commodities, these would increase modestly, by about seven percent. But for cotton, direct payments would increase by 66 percent (see page 4). An important reform in the proposal is to remove planting flexibility restrictions, which prevented farmers receiving direct payments from growing fruits and vegetables. The planting flexibility restrictions were successfully challenged in the Brazil WTO dispute on cotton, so this proposal would bring direct payments into compliance with that part of the Brazil case.

The Johanns proposal also adds a new, environmental component for direct payments, offering a ten-percent premium to farmers who implement a strategic conservation plan on their farms.

Payment Limits

The Johanns proposal also seeks to reform commodity subsidies by prohibiting subsidy payments to people with incomes over US$200,000 per year, based on a 3-year

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rolling average. In addition, it would eliminate loopholes that allow farmers to skirt existing payment limitations by creating multiple partnerships and corporations. Such loopholes now permit clever farmers to ignore payment limitations and take subsidies occasionally in excess of US$1 million.

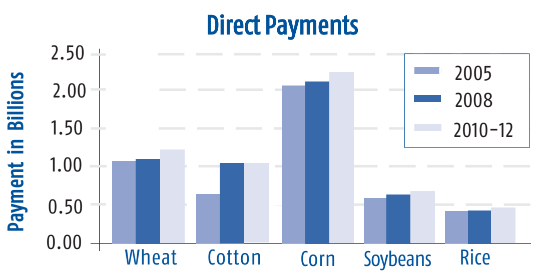
Sugar and Dairy

Sugar in the US is protected through a complex system of price supports and quotas. The US government manages supplies to keep internal prices high. The Johanns proposal recommends keeping the programme as is. However, since the North American Free Trade Agreement will open US-Mexico trade in 2008, Secretary Johanns proposes to reduce US domestic production if sugar imports exceed a set level. This will maintain higher domestic prices, even though Mexican sugar imports cannot be restricted.

Johanns also supports maintaining the Milk Income Loss Contract programme for dairy. This programme pays milk producers 34 percent of the difference between the market price and US$16.94 per cwt. The new MILC programme would phase down the payment rate to 20 percent by 2013 and set a historical production base. Payments would be restricted to the current volume limit of 2.4 million pounds per year, count towards a producer's overall annually counter-cyclical payment limit of US$110,000 and apply the US$200,000 income cap to MILC payments. This would make the programme more consistent with other counter-cyclical based payment programmes.

Cotton Shifts

Although the proposed reforms would have limited impacts on most commodities, those on cotton would be considerable. The trigger price for loan deficiency payments for cotton would be significantly reduced, from US$0.52 to US$0.39 per pound. Combined with other reforms, this would likely mean virtually no loan deficiency payments since cotton prices have rarely fallen that low.



To compensate for this change, the Johanns proposal includes a major increase – 66 percent – in direct payments for cotton. Under the 2002 Farm Bill, direct payments for cotton were approximately US$616 million each year. Under the Johanns proposal they would rise above US$1 billion annually (see graph below).

Green Payments and Social Issues

The Johanns proposal supports an additional US$7.8 billion for environmental conservation programmes, provides significant increases in research for bio-energy crops, creates new research and trade programmes for specialty crop producers, and devotes attention towards expanding federal funding for beginning, minority and socially disadvantaged farmers.

Food Aid

The Johanns proposal would authorise using up to one-quarter of US food aid budgets for local and regional purchase of food during emergency situations. Currently, virtually all US food aid is provided in the form of US commodities and transported on US-flagged ships. Although food aid has been a contentious issue in trade negotiations, the primary rationale for the proposed reform of food aid is to make US emergency food aid more flexible and responsive. Under any new WTO agreement, this form of food aid – emergency response – is likely to be exempted from new disciplines.

The Proposal and the Doha Round

At the time of this writing, many of the backup figures and assumptions that underlie the Johanns proposal had not been released to the public. Making precise assessments of its effects on subsidies, and on Doha negotiation positions, is therefore difficult.

As long as crop prices remain high, the proposal is more than likely to comply with US Uruguay Round commitment of US$19.1 billion in annual Amber Box support, and could reduce overall trade-distorting support below the US$22.5 billion a year offered by the US in October 2005. Lower prices, however, could trigger payments that exceed the offer. To remedy this, USDA has requested authority to adjust spending to comply with international obligations. It is unclear whether the USDA proposal is 'bold' enough to re-energise the Doha Round agriculture negotiations. Although Secretary Johanns has repeatedly emphasised that his proposal is *not* a new US negotiating offer, reactions in Geneva have been dubious.

The proposal recommends maintaining the sugar and dairy programmes at roughly similar levels, about US$1 billion for sugar and US$4.4 billion for dairy. Price support programmes for peanuts have been discontinued. Non-product-specific *de minimis* subsidies for water, crop insurance and disaster assistance vary, but figure in the neighbourhood of US$7 billion. Cotton payments triggered under the revenue-based counter-cyclical payment programme would be classified in the Blue Box.

Next Steps in Congress

Congressional reactions to the Johanns proposal have been neither very supportive nor very critical. Notably, the Democratic Chair of the Senate Agriculture Committee Tom Harkin welcomed the proposal and declared it 'not dead on arrival'. The Chair of the House Agriculture Committee Collin Peterson was less effusive, but said he was "pleased to see that Secretary Johanns included some good ideas in his proposals, even though there are some areas where we disagree," conceding that it was not as bad as he thought it was going to be.

The next important decision-point for the Farm Bill debate will be around budget matters, i.e. how much money is available. Congress is under pressure to reduce overall government spending, which could restrict the funding available to the 2007 Farm Bill. Key budget decisions will be made in March and April. When those decisions have been made, the House and Senate Agriculture Committees are expected to construct Farm Bill legislation in May through July, probably not concluding the process until September or October. Delays in any of these stages are quite possible.

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