APAC Agricultural Policy Analysis Center
The University of Tennessee

PolicyPennings by Dr. Daryll E. Ray

$500,000 in sales does not (usually) a viable net income make

In his February 24, 2009 speech before Congress, President Obama said, "In this budget, we will…end direct payments to large agribusinesses that don't need them." We were listening to the speech and when he said that we did a double take.

What did he mean?

Large agribusinesses like Monsanto, Cargill, ADM, AGCO, and Pioneer Seed don't receive direct payments. Direct payments are the current iteration of the AMTA (Agricultural Market Transition Act) payments that were made a part of the 1996 Farm Bill in order to entice farmers to support a radical reordering of farm programs. These payments are made to growers of the major crops (corn, soybeans, cotton, wheat, rice, etc.) so Obama wasn't talking about many large livestock producers, orchardists, and fruit and vegetable producers.

To our ears the wording was strange because, in most cases, we do not think of crop farmers, even the large ones, as "large agribusinesses." They may be incorporated to simplify tax and inheritance issues, but for the most part, they are family operations-hardly what comes to mind when the President talks about "large agribusinesses."

Our concerns were confirmed when word began to come out indicating that direct payments would be reduced for farm operators with over $500,000 in sales. Those numbers may seem large to someone earning $30,000 a year, but we have seen years where grain farmers with $500,000 in sales would have had a negative income if it hadn't been for farm program payments. Besides that, $500,000 in sales could often be achieved with fewer that 900 acres of corn OR fewer than 1700 acres of wheat, farm sizes that local farmers would definitely not consider "large."

While we are not fans of direct payments-preferring programs that deal with the causes of low prices and the need for a safety net-we believe that this proposal reflects a lack of understanding of agriculture on the part of some in the administration.

First, to fiddle with direct payments for farmers whose sales exceed $500,000 is to potentially reopen the 2008 Farm Bill. There are other programs that farmers would have negotiated if the $1.225 billion the Obama administration wants to save had been available for reallocation. The farm bill was put together by a bipartisan coalition and it may be as difficult to undo as the proverbial Gordian Knot.

Second, these "large" farms-those with over $500,000 in sales-produce 45.4 percent of the value of farm production in the US. Nearly 20 percent of all agricultural production is produced on farms with sales in excess of $1 million. These are the farms that produce the bulk of agricultural products in the US. The farms with sales in excess of $500,000 are the ones most likely to be able to employ a farmer or farm family members full time without dependence upon off-farm income.

That is not to say that there are not farm operations with less that $500,000 of sales that do make a viable living from farm sales, but those folks are likely not primarily growing crops that tend to have the most chronic price and income problems-that is, program crops.

Third, the current structure of many family farms reflects the requirements of a particular set of policy prescriptions. When those prescriptions change, one would expect to see changes in the organizational structure of family farms.

We looked at the farm structure of the largest recipients of direct payments (http://farm.ewg.org/farm/dp_analysis.php) and found what we expected. Most of them are family organizations that may include a farmer, her siblings, children, cousins and in-laws. The structure of many of these organizations reflect the triple entity rule of prior legislation with a farmer having 100 percent interest in one farm and half interest in two additional farms. These farm units of many related persons are then aggregated into the large farms that are called "large agribusinesses." They do this because they often share equipment, management decisions, and labor.

If the new regulations were put in place, we would expect to see the disaggregation of these units into smaller farms with sales levels under $500,000. If that were to happen the $1.225 billion in savings would disappear.

Fourth, a number of grain farmers who are eligible for direct payments also engage in livestock production. With a $500,000 sales limit in place, one would expect to see the non-grain operations like hog barns spun off into a separate enterprise under control of a single family member with the grain operations broken into units with less than $500,000 in sales.

It is our expectation that farmers are sitting down with their bankers, CPAs, and lawyers right now.

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Together they will develop farm structures that will meet the family needs of farmers while at the same time complying with gross sales limits.

Fifth, the suggestion that these farms could be paid for environmental services and earn income from energy production-solar, wind, and bioenergy-ignores the major causes of chronic price and income problems in the agricultural sector. One cannot expect payments for environmental services to cover problems caused by long periods of low prices followed by a short-term spike in prices and a subsequent return to low prices and high production costs.

As for bioenergy crops, one must understand that in part profitability in this arena is dependent upon uncertain oil prices.

Solar and wind energy production depend upon the availability of access to electrical grids which cannot be built by individual farmers. In addition, as long as priority access to electrical grids is given to "dependable" coal fired plants instead of intermittent wind and solar sources, the profitability of wind and solar is in question.

If farmers are going to be encouraged to bank on the "green" production of wind and solar energy, then they must be given priority on the electrical grid, with wind and solar generators in other areas and peaking plants being used to cover the down times.

Obama's stated intent is to tilt economic policies to favor the middle class, those earning less than $250,000 per year. The $500,000 in farm sales rule seems to violate that intent. It dumps agriculture's sizable middle class in with the few truly big boys.

If eliminating direct payments and/or other payment programs is an Obama administration goal, then the justifications and suggested alternative income sources need to be credible and an outline of a substitute means to address chronic market imbalances in crop agriculture should be suggested.

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