House Ag Committee proposes raising reference (target) prices following periods of “high” prices

On April 12, 2018, members of the House of Representatives Agriculture Committee received a copy of the 2018 Farm Bill proposal, the Agriculture and Nutrition Act of 2018. A sign of the hopes for the legislation and its quick passage could be found in its number, H.R.2—the tax cut legislation was H.R.1.

But hopes for the bi-partisan support that typically greets new farm bills were quickly dashed by the announcement that the Ranking Member of the Agriculture Committee, Colin Peterson was withholding his support for the bill. In some ways the introduction was similar to the situation surrounding the introduction of the 2014 Farm Bill when House Republicans split the Farm Bill in two—one bill for agriculture programs and another for nutrition programs.

In both cases, part of the strategy was to make cuts to nutrition programs, a particular focus of Tea Party Republicans. The Democrats resisted then and they are currently resisting such cuts. The lack of bi-partisanship could be seen in the Agriculture Committee where the Chair, Michael Conaway, declared that no amendments to the submitted legislation would be accepted from anyone who was not going to vote yes on legislation. The bill passed out of committee on a party line vote on April 18.

Because we expect that the issues with the nutrition title will come into sharper focus in the next few months, we want to turn our attention to the Price Loss Coverage (PLC) program. With crop prices below the reference prices included in the 2014 Farm Bill, it is expected that many of the farmers who elected to participate in the Agricultural Risk Coverage (ARC) program following the adoption of the 2014 legislation will elect to participate in PLC this time around.

In the run-up to the introduction of the 2018 Farm Bill, legislators said that they were not looking to make major changes to commodity programs, but that farmers could expect enhancements to the 2014 legislation to improve farm safety net programs. We expected that the Agriculture Committee would tinker with the reference price and maybe find ways to make partial payments to farmers during a crop year with prices below the reference price—a time when extra income is needed—instead of after the end of the crop year. They did the first and we have found no indication that they did the second—we haven’t made it all the way through the 641 pages of H.R.2.

The proposed farm bill introduces the concept of the “effective reference price.” According to H.R.2, “the term ‘effective reference price’, with respect to a covered commodity for a crop year, means the lesser of the following: (A) An amount equal to 115 percent of the reference price for such covered commodity. (B) An amount equal to the greater of—(i) the reference price for such covered commodity; or (ii) 85 percent of the average of the marketing year average price of the covered commodity for the most recent 5 crop years, excluding each of the crop years with the highest and lowest marketing year average price [Olympic average price].”

The reference price was set in the 2014 legislation and for illustrative purposes we will look at corn with a reference price of $3.70 per bushel. The effective reference price allows the price on which payment calculations are made to increase to as high as 115 percent of the reference price.

At this point we are going have to get into the mathematical weeds to sort out what this means for a typical crop (it took us an Excel spreadsheet to figure this out). For our typical crop we will use corn since that is the major crop produced on US farms.

Let's start with B(i), the reference price in the legislation. For corn this is $3.70 per bushel.

Now, let's look at A which is 115 percent of the reference price. For corn this is $4.255.

Next, we must calculate the point at which 85 percent of the 5-year Olympic average B(ii) is greater than B(i). That means that for corn the 5-year Olympic average must be greater than $4.353 or the effective reference price will be the reference price of $3.70.

Lastly, we need to calculate the point (Bii) at which 85 percent of the 5-year Olympic average price exceeds A. As we have seen, for corn point A is $4.255 and the last point at which B(ii) is less than A is $5.006. Between those two Olympic average prices, the "effective reference price" will range from a low of $3.71 to a high of $4.255.

That means that starting from a low-price period like the 2013-2017 crop years, as long as the season average price stays below $4.35, the effective reference price will remain at $3.70. Even a one-year price above $4.35 will provide no benefit in the first year, because the high price year and the low-price year are excluded from the calculation of the Olympic average.

It will take multiple years with corn prices above $4.35 to increase the "effective reference price." And if the price is near or above the full cost of production, is PLC needed at all?

At its best, the House of Representatives Agriculture Committee's proposed 2018 Farm Bill will provide the best benefits if the Olympic average corn price reaches $5.01 and then begins to decline.

What farmers need right now is not the promise of a benefit sometime in the future, but rather a program that will lift prices and enable them to earn their living from the marketplace.

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