

THE COST OF AMERICA'S FARM SUBSIDY BINGE: AN AVERAGE OF \$1 MILLION PER FARM

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As Congress is locked in debate on the best way to stimulate an economy that has slipped into recession, the House and Senate have designed farm bills that will place inordinate burdens on American taxpayers, countering stimulus efforts while providing payments to many farm owners who are least in need of assistance. The Senate farm bill (S. 1731, formerly S. 1628) is expected to entail annual costs similar to those of the Farm Security Act (H.R. 2646) passed by the House of Representatives by a vote of 291 to 120 on October 5. The House farm bill would allow payments averaging more than \$1,000,000 to full-time farms over the next 10 years, leaving the average household with \$4,377 less to spend, save, or invest throughout those years.

The most expensive farm legislation in the history of any nation, the Farm Security Act would result in a total of \$190 billion in taxes on American families and an additional burden of \$271 billion in inflated food prices. Purportedly, this \$461 billion expenditure would be incurred to help struggling farmers and stabilize food prices; in reality, however, it would accomplish neither of these goals.

Instead, the money would be channeled into programs that are confused, contradictory, and counterproductive and would leave acres of fertile land lying idle. Many of the beneficiaries of these programs would be large-scale farmers and agribusinesses with million-dollar incomes and per-unit production costs that are one-third those of smaller farms. Enactment of the Farm Security Act or its Senate version would not serve the interests of the nation's taxpayers or its wobbling economy.

RETREAT FROM REFORM

The Farm Security Act represents the final abandonment of the 1996 Federal Agricultural Improvement and Reform Act (P.L. 104-127), which once provided hope of reform in a dismally failed system

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of farm subsidies. This bill, known as the Freedom to Farm Act, gave farmers more control over their planting decisions in return for fewer subsidies.

Farmers enjoyed Freedom to Farm's flexibility, but when crop prices dipped slightly, the farm lobby reverted to its former response, demanding (and receiving) billions in annual "emergency" farm subsidies. Agriculture lobbyists were willing to trade farmers' freedom for the security that only guaranteed taxpayer-funded handouts can provide, and today, the Freedom to Farm initiative has been completely abandoned.

Both the House and Senate bills would provide permanent support to farmers in four major categories:¹

- **Farm subsidies and loans.** The 1996 Freedom to Farm Act was an important step toward phasing out subsidies and loans that were based on specific crops and acreage levels and, in essence, dictated farmers' planting decisions. These payments were replaced with production flexibility contracts (PFCs), which were fixed payments that did not require farmers to plant certain crops and did not fluctuate with crop prices. PFC payments were intended to decrease annually until they were phased out, leaving farmers off the dole once and for all. Both H.R. 2646 and S. 1731 would reverse this move toward reform. Rather than phasing out PFCs, they would extend them permanently with expansions into new crops while reintroducing the old economy-distorting crop-specific payments as "countercyclical payments." In addition, both bills would continue to fund non-recourse loans which, despite their name, function as grants to farmers in the event that crop prices fall. According to the Congressional Budget Office, the Farm Security Act would add \$50 billion in these subsidies and loan expenditures to the \$70 billion that is already committed over the next decade.
- **Conservation payments.** The Conservation Reserve Program (CRP) pays farmers to sign 10-

year contracts promising *not* to farm their land, ostensibly for the purpose of environmental restoration, and also to substantially raise food prices by decreasing the amount of crops grown. Both the House and Senate farm bills would increase the number of acres enrolled in the CRP from approximately 36.4 million to nearly 40 million. Largely as a result of the CRP, the Farm Security Act would increase the costs of conservation programs to taxpayers by \$35 billion over the next 10 years.

- **Price supports.** Both the House and Senate bills would continue price support programs that raise the prices of the agricultural products such as sugar and dairy products to artificially high levels. These high prices are achieved through import restrictions, marketing quotas that limit who can grow certain crops and how much they can grow, and even outright government purchases of crops to remove products from the market before an excess of supply can lower prices. Both farm bills would retain most price support programs while replacing peanut price supports with direct payments to peanut farmers, shifting the peanut program's cost from consumers to taxpayers. It is projected that increased food costs resulting from price support programs and the Conservation Reserve Program will cost consumers \$271 billion over the next decade.
- **Crop Insurance.** Farmers receive catastrophic insurance that is virtually free for most crops grown. Farmers who opt to purchase additional coverage would have a substantial portion of the premiums paid by the federal government. Crop insurance payments are expected to cost more than \$36 billion over the next 10 years.

All told, farm policy after the Farm Security Act will cost Americans \$190 billion in taxes and \$271 billion more in inflated food prices over the next 10 years for a total cost of \$461 billion. During that period, the federal government will allocate an average of \$1,012,375 (\$417,509 in subsidies and \$594,866 in price supports) to each of the approxi-

1. Because cost estimates of S. 1731 have yet to be released by the Congressional Budget Office, all cost estimates refer to H.R. 2646. However, it is estimated that both bills will cost roughly the same amount per year. All cost estimates are justified in the appendix.

mately 456,000 full-time farms in the United States.² Paying this enormous tab will cost the average household \$1,805 in taxes and \$2,572 in inflated food prices for a total 10-year cost of \$4,377.

However, these cost estimates assume that current budget projections are accurate when, in reality, expenditures could be much higher. Since 1990, annual “emergency payments” to farmers have increased the amount of government farm payments by 67 percent over projected expenditures.³ If Congress continues to approve multibillion-dollar annual emergency packages in addition to payments included in the annual budget, the total costs of farm support could top \$6,000 per household throughout the next decade.

PROGRAMS WITHOUT A PURPOSE

Most taxpayers do not object to paying for government programs that confront pressing national needs with lean, efficient, workable solutions. The current farm bill, however, is not only a solution in search of a problem, but also a remedy that lacks any grounding in either logic or economics.

Historically, farm subsidies have been defended as necessary to stabilize food prices and supplies, as well as to support farmer incomes. While these justifications were valid when the paradigm for the government’s agricultural policy was created several generations ago, they are no longer valid in 2001. Because supply disruptions and their consequent surpluses and shortages manifest themselves in

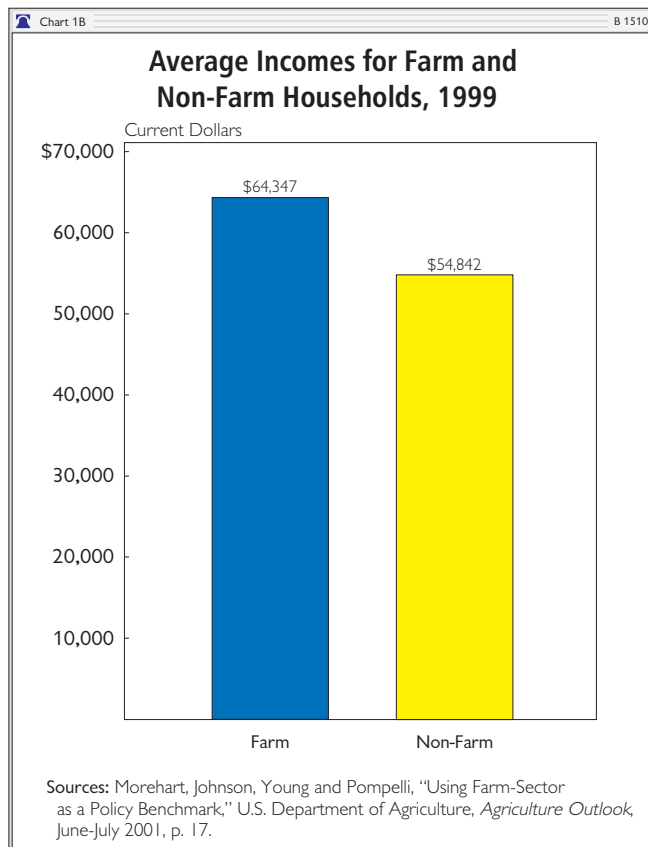
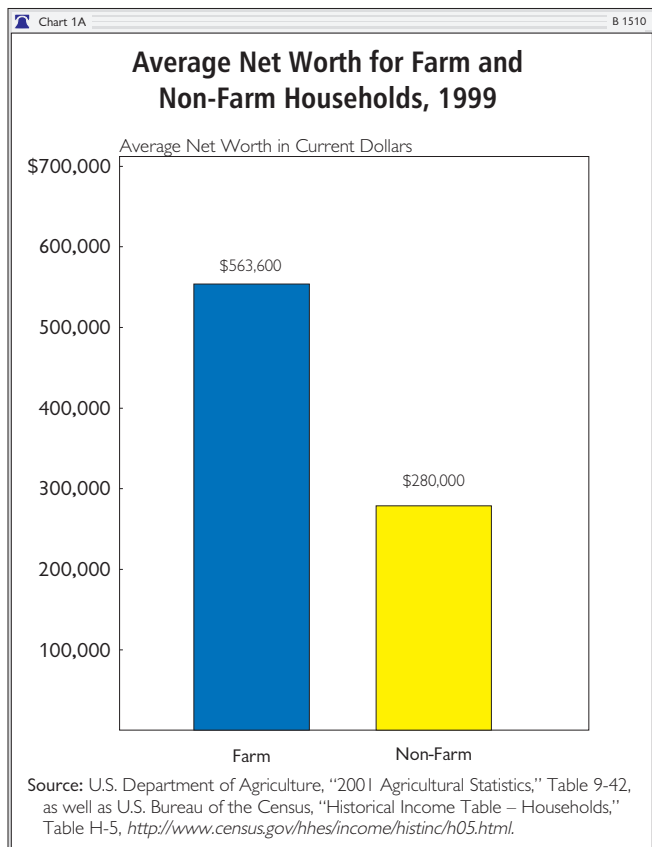
rapid but lengthy price swings, the long-term stability of food supplies can be examined best through trends in food prices and expenditures.

Although farm policies and the crops affected have changed dramatically over the past century, food prices have remained relatively stable, growing at an average annual rate just under the consumer price index (CPI).⁴ Accordingly, food expenditures also have grown at a steady level, trending slightly under the annual growth of personal income. This trend has allowed the percentage of disposable personal income spent on food to drop from 25 percent in 1933 to just over 10 percent in 2000.⁵ It is reasonable to conclude that food supplies and prices have remained stable regardless of agricultural policy and that, with food becoming an increasingly small percentage of family expenditures, the impact of any future price fluctuations on consumers would be minimal.

2. Full-time farms are defined as those with over \$50,000 in annual revenues, which receive nearly 90 percent of all farm benefits.
 3. Compiled by author using *Historical Tables: Budget of the United States Government, Fiscal Year 2002*, budget function 351, as well as the 1990 and 1996 farm bill cost estimates provided by the Congressional Budget Office.
 4. Council of Economic Advisers, *Economic Report of the President, February 2001*, Table B-60, as well as data provided by the Bureau of Labor Statistics.
 5. *Ibid.*

Table 1				B 1510
Total Transfers to Farmers Under H.R. 2646				
Combined Amounts over 2002–2011				
<i>(In billions of dollars unless otherwise noted)</i>				
	Current projections	HR 2646 additions	Total	
Taxpayer payments to farmers	\$128.1	\$62.3	\$190.4	
Higher consumer prices paid to farmers	\$274.9	-\$3.6	\$271.3	
Total transfers to Farmers	\$402.9	\$58.7	\$461.6	
Number of full-time farms			456,000	
Average transfers per full-time farm (in actual dollars)			\$1,012,375	
Number of households			105,480,101	
Average cost per household (in actual dollars)			\$4,377	

Notes: Some amounts may not sum due to rounding. See appendix for complete summary of calculations.



Even if it is assumed that some mechanism is needed to ensure price and supply stabilization, the government's current farm policy is too flawed to accomplish this goal. Logic dictates that a price stabilization policy should be countercyclical, raising crop prices when they are too low and lowering farm prices when they are too high.

In contrast, all of the farm policies that have been adopted to affect market prices—such as price supports and conservation payments to keep land idle—are designed only to raise prices above the market-clearing level; they cannot drop prices below it. Rather than experiencing the stabilization of prices and supplies, American consumers face only price increases. Consequently, there is no evidence that the few dozen subsidized and supported crops have had prices or supplies any less stable

than the nearly 400 unsubsidized crops over the past century.⁶

In truth, food prices and supplies do not require government stabilization any more than industries such as technology, energy, and telecommunications do. Nor do today's farmers need income supports more than those engaged in any other occupation do. When large-scale farm subsidies were created in the 1930s, farmer income was only approximately 50 percent of the national average. Today, the average family farm has a household income of \$64,347 (17 percent above the national average)⁷ and a net worth of over \$563,600 (double the national average), which is even more impressive considering that the cost of living in rural areas is 10 percent to 40 percent lower than in urban areas.⁸ Farms fail at only one-sixth the rate of

6. John Frydenlund, *Freeing America's Farmers: The Heritage Plan for Rural Prosperity* (Washington, D.C.: The Heritage Foundation, 1995), pp. 46–48.

7. U.S. Department of Agriculture, *2001 Agricultural Statistics*, Table 9–42, as well as U.S. Bureau of the Census, "Historical Income Table—Households," Table H–5, at <http://www.census.gov/hhes/income/histinc/h05.html>.

8. Mitch Morehart, James Johnson, C. Edwin Young, and Greg Pompelli, "Using Farm-Sector as a Policy Benchmark," U.S. Department of Agriculture, *Agriculture Outlook*, June–July 2001, p. 17.

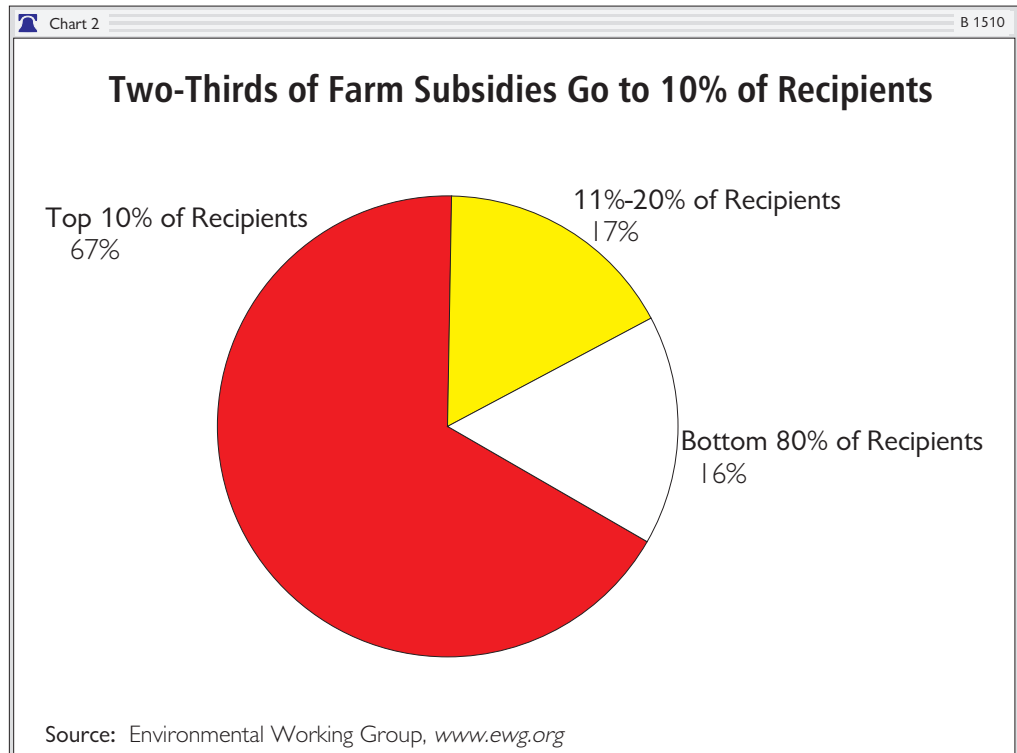
non-farm businesses, and only 4.5 percent of farms have enough debt to be considered vulnerable to bankruptcy.⁹ Yet Congress still votes to transfer hundreds of billions of dollars to farmers.

Not only is the rationale for subsidizing the agriculture industry questionable, but the impact of government subsidies is dubious. Although the vast majority of farms are doing well financially, the growers of unsubsidized crops actually have enjoyed faster-rising incomes than subsidized farmers; the absence of government intrusion proved to be more important to farmers' success than subsidies.¹⁰ The innovation and responsiveness to the market exhibited by unregulated farmers were major factors in the 22 percent increase in farm productivity over the past decade—a rate that bodes well for their continued financial success.¹¹ By all indications, the farming industry will be able to continue thriving without unneeded and counterproductive farm subsidies.

The very small percentage of farmers who truly are struggling financially can expect little help from federal agriculture programs, which direct a vast majority of the money to large farms and agribusinesses that, as a result of per-unit production costs often one-third those of smaller farms, already earn

millions annually before farm subsidies.¹² Current farm policies offer subsidies to only 40 percent of farms, and the Environmental Working Group, a nonprofit environmental research organization, reports that two-thirds of all farm subsidies go to just 10 percent of these qualified recipients.¹³

If current trends continue, this small cadre of subsidy recipients (which includes Members of Congress, *Fortune* 500 companies, and multimillionaire “hobby farmers” such as Ted Turner, Scott Pippen, and David Rockefeller) can expect a \$308 billion windfall over the next decade, and large subsidies will continue to dwarf the \$935 median annual subsidy that most subsidized farmers can expect.¹⁴



9. Jerome M. Stam, Daniel L. Milkove, and George B. Wallace, “Indicators of Financial Stress in Agriculture Reported by Agricultural Banks, 1982–99,” U.S. Department of Agriculture, Economic Research Service, AIS–74, February 2000, p. 48, and data provided by U.S. Department of Agriculture at <http://www.ers.usda.gov/Briefing/FarmFinancialMgmt/brief99.htm>

10. James Bovard, “Farm Bill Follies of 1990,” *Cato Policy Analysis* No. 135, July 12, 1990.

11. U.S. Department of Agriculture, *2001 Agricultural Statistics*, Table 9–26.

12. Linda Foreman, “Characteristics and Production Costs of U.S. Corn Farms,” U.S. Department of Agriculture *Statistical Bulletin* 974, August 2001, at <http://www.ers.usda.gov/publications/sb974-1/sb974-1.pdf>.

13. Data provided by the Environmental Working Group, at www.ewg.org.

14. *Ibid.*

FUNDAMENTALLY FLAWED PROGRAMS

Another major problem that characterizes farm subsidy programs is that their very design is fundamentally flawed and makes no economic sense. Farm policy is based on the assumption that the market prices of crops are too low for farmers to earn sufficient revenue. Because food demand is relatively inelastic (i.e., not very price sensitive), low prices are the result of an oversupply of crops on the market.

Congress's remedy for low prices is counterproductive and ultimately aggravates the cause of the problem. As laid out in H.R. 2646 and S. 1731, the government's approach is to set a higher target price for farmers to receive, and then to supplement farmers' incomes by paying them the difference between the target prices and the low market prices. Not surprisingly, such subsidies provide farmers with an incentive to grow *more*, not less, of the oversupplied crops. In fact, farmers have responded to past subsidies by planting as many as 5 million acres *more* of the oversupplied crops, driving prices down further and necessitating even higher subsidies.¹⁵

Adding to the problem, farm policy has been contradictory, and its various programs serve conflicting purposes. For example, while the federal government is offering billions of dollars in programs that provide incentives for farmers to grow more of the crops that are already in oversupply, the Conservation Reserve Program is sending other farmers billions of dollars in return for *not* farming almost 40 million acres of land—the equivalent of idling every farm in Ohio, Indiana, Michigan, and Wisconsin.

While the CRP is much more successful at raising prices than crop-based subsidies, its inefficiency is even greater than that of the subsidy programs. Crop subsidies and price supports cause marginal inefficiencies by shifting land to crops that are less in demand, but the CRP takes productive farmland completely out of production, thereby creating a “deadweight loss” on the economy that costs well

over 100,000 potential jobs and billions of dollars in lost output annually.¹⁶ Paying some farmers subsidies to grow more crops and other farmers subsidies to grow fewer crops—each at high taxpayer costs—is characteristic of this self-defeating “one foot on the accelerator, one foot on the brake” farm policy.

The burdens on Americans of these high-cost inefficient programs do not end with crop payments and the CRP. After taxpayers have paid billions in taxes for programs that increase the price of food, they then, as consumers, must suffer those price increases at supermarkets and restaurants. H.R. 2646 would lead to \$271 billion in artificially high food prices over the next decade at an average household cost of \$2,572 that would disproportionately burden the poor. These higher food prices would generate a ripple effect in tax increases by boosting the costs of government-provided food programs, such as food stamps, WIC, and school lunches.

The artificially higher prices would also price U.S. agricultural commodities out of foreign markets, forcing taxpayers to pay an additional \$1 billion in annual crop export subsidies to lower the international prices of the food they had just paid taxes to increase. Finally, taxpayers can expect to fund additional “emergency payments,” which in recent years have doubled the federal cost of agricultural policy. Although emergency payments are intended to be limited to natural disasters, farmers often receive payments whether the weather is good or bad for farming. If the weather is bad, destroyed crops necessitate disaster payments; if it is good, a surplus in supply lowers prices and requires increased farm subsidies and price supports. Once again, the taxpayers lose either way.

The agricultural policies that H.R. 2646 and S. 1731 would extend through 2011 are a contradictory, confused mess, currently requiring nearly 100,000 Department of Agriculture employees—one for every four full-time farmers—just to interpret and implement. Despite the complexity of these programs, as well as their inherent contradic-

15. Paul C. Westcott and C. Edwin Young, “U.S. Farm Program Benefits: Links to Planting Decisions and Agricultural Markets,” U.S. Department of Agriculture, *Agriculture Outlook*, October 2000, p. 13.

16. U.S. Department of Agriculture, “Final Regulatory Impact Analysis—1987 Farm Commodity Programs,” p. 1.

Table 2 B 1510

The Contradictory Yet Expensive Results of Farm Policy

Policy	Output	Prices	Taxes
Farm Subsidies and Loans	↑	↓	↑
Price Supports	↓	↑	↑
Conservation Reserve Program	↓	↑	↑
Export Subsidies	↑	—*	↑
Net Impact	Undetermined	\$271 billion	\$190 billion

Note: * Prices decrease for foreigners purchasing American exports, but domestic prices remain unchanged
Source: Author's calculations

tions that cause one program to cancel out the impact of another, they all have one main result: substantially higher taxes and food prices.

A BETTER WAY

Representative Charles Stenholm (D–TX), the ranking member of the House Agriculture Committee, calls the Farm Security Act “a good deal for agriculture and a good deal for taxpayers.” Certainly, farmers would enjoy the \$1,012,375 in benefits they would average over the next decade. Taxpayers, on the other hand, would be saddled with a \$190 billion tax tab with nothing to show for their taxes except \$271 billion in higher food prices.

The current Freedom to Farm legislation does not expire until September 30, 2002. Congress should step back and spend the next 10 months crafting an agricultural bill based on the following four principles:

- Just as central planning has failed across the globe, centralized farm policies cannot allocate

resources with the efficiency of the free market.

- Farmer incomes and net worth are not low enough to necessitate large-scale farmer welfare, and there is no justification for taxing working Americans and inflating food prices to subsidize multimillionaires.
- Agriculture is no more prone to major disruptions in prices and supplies than other industries such as telecommunications, technology, or energy, and any short-term risk can be addressed through crop insurance and commodity futures markets.

- Policies discouraging production and raising food prices prevent American farmers from taking advantage of rapidly expanding global export markets.

A good starting point for reform can be found in S. 1571, a farm bill offered by Senator Richard Lugar (R–IN) that would phase out most crop subsidies and price supports, and instead help farmers manage short-term risk by offering federal subsidies for farmers to purchase crop insurance. This approach would be an important first step in freeing America’s agriculture industry and reducing the burden of taxpayers and consumers who are currently paying billions of dollars to subsidize multimillionaires.

That would be a *real* economic stimulus.

—Brian M. Riedl is Grover M. Hermann Fellow in Federal Budgetary Affairs in the Thomas A. Roe Institute for Economic Policy Studies at The Heritage Foundation.

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Total Transfers to Farmers Under H.R. 2646			
Combined Amounts over 2002–2011			
<i>(In billions of dollars unless otherwise noted)</i>			
Taxpayer Payments to Farmers¹			
	Current projections	HR 2646 Additions	Total
Direct commodity payments	\$69.9	\$49.8	\$119.7
Crop insurance	\$36.7	-	\$36.7
Conservation payments	\$21.5	\$12.5	\$34.0
Total taxpayer payments to farmers	\$128.1	\$62.3	\$190.4
Higher Prices Paid to Farmers			
Projections based on current policies			
Estimated food expenditures, 2002–2011 ²			\$10,572.7
Higher prices as a percentage of food expenditures ³			2.6%
Subtotal			\$274.9
Major H.R. 2646 provisions affecting prices			
Replace peanut quota with direct payments to peanut farmers ⁴			-\$4.1
Terminate Northeast Dairy Compact ⁵			-\$0.7
Add 2.8 million acres to the Conservation Reserve Program ⁶			\$1.2
Subtotal			-\$3.6
Total higher prices paid by consumers			\$271.3
Summary			
	Current projections	HR 2646 additions	Total
Taxpayer payments to farmers	\$128.1	\$62.3	\$190.4
Higher consumer prices paid to farmers	\$274.9	\$3.6	\$271.3
Total transfers to Farmers	\$402.9	\$58.7	\$461.6
Number of full-time farms⁷			456,000
Average transfers per full-time farm (in actual dollars)			\$1,012,375
Number of households⁸			105,480,101
Average cost per household (in actual dollars)			\$4,377
Note: Some amounts may not sum due to rounding			
Sources:			
1. Baseline estimates and H.R. 2646 cost estimates for Titles I and II provided by the Congressional Budget Office.			
2. Westcott, <i>USDA Agricultural Baseline Projections to 2010</i> , U.S. Department of Agriculture, February 2001, Table 34. An estimate for 2011 was calculated by projecting a 3.8% increase over 2010, which is the average annual growth rate throughout the baseline.			
3. Organisation for Economic Co-operation and Development, <i>Agricultural Policies in OECD Countries: Monitoring and Evaluation 2001</i> . Table III.44 shows transfers from consumers to producers through artificially high prices averaged 2.6 percent of all American food expenditures from 1998-2000.			
4. U.S. General Accounting Office, <i>Peanut Program: Impact on Peanut Producers, Users, and the Government</i> , T-RCED-95-215, June 8, 1995, p. 6. This report shows that several USDA calculations of the annual consumer cost of the peanut program have an average value of \$414 million. Therefore, eliminating the program would save consumers approximately \$4.14 billion over 10 years.			
5. Rich Zipperer, "Who's Raising Milk Prices," Consumer Alert, www.consumeralert.org/pubs/research/August97.htm . This estimates the Northeast Dairy Compact's consumer cost at \$67 million annually, or \$670 million over 10 years.			
6. Peter Feather, Daniel Hellerstein, and LeRoy Hansen, <i>Economic Valuation of Environmental Benefits and the Targeting of Conservation Programs: The Case of the CRP</i> , U.S. Department of Agriculture, AER Report #778, April 1999, p. 6. Estimates reveal the CRP costs consumers an average of \$421 per acre over 10 years. H.R. 2646's addition of 2.8 million acres to the CRP will therefore cost consumers \$1.179 billion over 10 years.			
7. U.S. General Accounting Office, <i>Farm Programs: Information on Recipients of Federal Payments</i> , GAO-01-606, June 23, 2001, pp. 1-2. Full-time farms are defined as those with annual gross sales of at least \$50,000, generally considered an appropriate cutoff separating full-time farmers from "hobby farmers." Farmers with sales over \$50,000 account for almost 90 percent of all annual farm production, and receive almost 90 percent of all farm subsidies and price supports.			
8. U.S. Bureau of the Census, "Census 2000," Summary File 1, Table P-1.			