Testimony

Of

Pam Johnson
First Vice President, National Corn Growers Association

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Madam Chairwoman, Ranking Member Roberts and members of the Senate Agriculture Committee, on behalf the National Corn Growers Association (NCGA), I appreciate the opportunity to share with you our views on the importance of sound risk management programs to family farms as you begin your deliberations on writing the 2012 Farm Bill.

My name is Pam Johnson. I am a 6th generation farmer from Floyd, Iowa where I raise corn and soybeans with my husband and 2 sons. I currently serve as First Vice-President of NCGA.

The National Corn Growers Association represents more than 36,000 corn farmers from 48 states. NCGA also represents more than 300,000 corn growers who contribute to check off programs and 27 affiliated state corn organizations across the nation for the purpose of creating new opportunities and markets for corn growers.

As this Committee and the Congress consider legislation to authorize a new farm bill, NCGA believes it is very important to remember that U.S. agriculture must be prepared to take on an even greater role in meeting the growing demands of world consumers. The harsh reality is that billions of people in the world today remain hungry and the numbers are rising, a trend the Food and Agriculture Organization of the United Nations reports will continue for another 30 years. We simply cannot afford to underestimate these challenges as well as the market opportunities in a world where 95 percent of the population lives outside the United States. NCGA is confident that the U.S. agriculture sector can remain a vital bright spot in our nation's economy and further contribute to its recovery.

Fortunately, advances in seed technologies along with modern production and conservation practices have generated substantial increases in productivity that will help meet the pressing need for an expanding food supply. In fact, the average bushels per acre increased from 114 in 1995 to 153 in 2010, a productivity increase greater than 30 percent. These remarkable numbers and the promise of new production technologies on the horizon translate into U.S. corn growers' ability to meet all our needs for food, feed, fuel and fiber. NCGA would argue that these investments in an industry fraught with financial and production risks have been made possible in large part by a reliable farm safety net with the cost share federal crop insurance program as the foundation.

In light of the extremely difficult fiscal and economic conditions that our nation faces today, NCGA recognizes the monumental task before this committee to advance a new farm bill that must address a broad range of nutrition and agriculture concerns across the country. Our growers also understand they must be part of the solution to address our nation's unsustainable budget deficits and are prepared to accept appropriate spending reductions in farm programs. In preparation for this new budget reality, NCGA initiated internal discussions over two years ago on how to improve upon the market oriented reforms in the commodity title. These ongoing discussions have been augmented by substantial independent analysis of suggested changes to existing farm programs and new concepts considered by our Public Policy Action Team.

First and foremost, NCGA cannot overemphasize the consensus among our membership that the federal crop insurance program is the most critical risk management tool for their farm operations. Why is federal crop insurance important to me and other farmers? When we go to

the field this year to plant, tend and harvest a crop, we are putting many dollars, a whole year's work and our entire yearly income at risk. Traditionally, we worry about the risks from drought, floods, storms, plant disease, and pestilence to crops in the field, but now the risks are not just physical. Interconnected global markets that have benefited agriculture are now also a source of peril: international incidents, economic crises around the world, currency exchange rates, global monetary and trade policies, embargoes, the price of a barrel of oil and the list goes on. We may do everything right with our management practices and the decisions that are within our control on the farm, but there are years when we cannot adequately cover our losses from all the risks, seen and unseen.

These threats are hard on farmers like me, but even more so for the young farm families like my two sons who are just getting started in agriculture. Access to a crop insurance plan is even more critical in times like these to help farmers face the agronomic perils and the uncertainty of the marketplace. We believe it is key to the foundation of a good farm bill.

From a larger perspective, the extreme volatility in the commodity markets experienced over the past five years as well as the impact of major flooding in the Midwest and severe drought conditions in the South remind us that the risks in farming are expansive and immediate. The corn industry has certainly enjoyed considerable improvement in prices, but growers continue to confront the pressures of rising input costs and increasing land rents as competition for inputs bids up prices. Federal crop insurance, especially revenue protection coverage, has proven to be the most flexible and market oriented risk management tool for protecting family farm income; it has permitted growers to insure adequate revenue to cover that year's cost of operation.

For the 2011 crop year (as of March 5, 2012), 78.07 million acres of corn were insured under the federal crop insurance program for liability protection of $51.48 billion compared to 73.5 million acres for $31.6 billion of protection the previous year. The premiums paid to insurance providers for corn policies totaled $4.75 billion with producers responsible for an estimated 40 percent of the program's total premium. In terms of sheer volume and total liability protection, it should be no surprise why NCGA is committed to working with the Risk Management Agency to ensure that the program is administered as efficiently and equitably as possible.

Consequently, we were pleased by the Department of Agriculture's decision late last year to begin a phase-in of long overdue changes in the rating methodology to better reflect the actual loss experience in the premiums paid for corn policies. Full implementation of the rating methodology changes by the RMA is necessary for the rating of corn policies to more accurately reflect reduced yield variability, yield trend increases and appropriate weighting corrections. Otherwise, the rating system will continue to set premiums well above corn's loss experience that has been documented over the past fifteen years.

While individual federal crop insurance policy coverage provides very effective assistance if revenue or yield decline between planting and harvest, it is limited to each policy's insurance year and is insufficient to insure adequate return on investment over the intermediate term, such as for equipment. Crop insurance is simply not designed to address price-induced declines in revenue that can last several years. Extended periods of low revenue can result from successive years of price declines or multiple years of below average production or "shallow losses" not

covered by crop insurance. Recall the depressed markets from the grain demand collapse of the early 1980's and the Asian financial crisis of the late 1990s. These unfortunate events can and do result in a gradual, but serious erosion of a farmer's equity.

To address these gaps in protection against significant production shortfalls and volatile markets, NCGA has advocated for a more market-oriented, revenue-based risk management program that complements crop insurance. In our view, the ad hoc disaster assistance packages approved in the past in response to these situations were not only poorly targeted but also inequitable. A 2009 USDA Economic Research Report indicates that a revenue-based support program can "be more efficient than the traditional suite of uncoordinated commodity programs and disaster assistance programs in that payments are more closely aligned to actual changes in farm revenue. If prices and yields are inversely related, the revenue-based approach may offer less variable payment outlays from year to year than the long standing forms of support—even if mean total payments are the same between the two forms of support. In such a case, a high level of payments may also be less likely under revenue-support."[1]

The efficiency of revenue programs led NCGA to support the Average Crop Revenue Election Program adopted in the 2008 Farm Bill. ACRE represents a fundamental reform to the farm safety net; one that NCGA believes provides a more responsive risk management tool for rising input costs, improving yield trends and greater market volatility. To date, over 136,170 farms have enrolled in the program comprising almost 13 percent of base acres. Although the program's design and administration has been subject to criticism, the fact is ACRE has delivered some much needed assistance to producers across the country.

In response to grower concerns, NCGA has recommended that a new revenue based program include these proposed changes. 1) Set the revenue benchmark at the Crop Reporting District to better address area wide disaster related production losses closer to the farm. 2) Use a simple 5 year Olympic Average Revenue rather than separate price and yield formulas which cause considerable confusion. 3) Base payments on planted acres rather than base acres. 4) Lower the maximum payment level to ensure optimal protection against "shallow losses" and to eliminate overlap with crop insurance. Independent economic analysis of these recommended changes to ACRE indicates substantial savings for deficit reduction and a more effective revenue based risk management program for protection against multiple years of declines in revenue for most crops.

NCGA believes the legislation introduced by Senators Sherrod Brown, John Thune, Richard Durbin, and Richard Lugar-the Aggregate Risk Revenue Program-best incorporates the principles of a market-oriented, revenue-based risk management approach while addressing some of the noted problems experienced with the ACRE program. NCGA has made it clear that we do not promote programs that would encourage farmers to take on unnecessary risk. A number of agriculture economists are stating that ARRM would not result in moral hazard or adverse selection since the revenue is measured at the Crop Reporting District level and prices are effectively national. The ARRM proposal is designed to partially offset losses not covered by crop insurance and to mitigate sharp year-to-year declines in price that crop insurance does not. NCGA understands farmers need to be able to sustain a certain amount of loss in any one

[1] Cooper, J. 2009. *Economic Aspects of Revenue-Based Commodity Support*, ERR-72, U.S. Department of Agriculture, Economic Research Service, April.p. 1.

year. It is very important that we try to protect farmers, especially young farmers, from depleting their emergency funds when they encounter revenue losses over a period of multiple years.

The revenue programs described in the 2009 USDA analysis are different from the current ACRE and other revenue based proposals for the 2012 Farm Bill and thus the specific provisions of revenue programs may result in significant differences in results. Nonetheless, the results illustrate the advantages of revenue-based programs over price-based programs such as the Counter Cyclical Payment (CCP) and Marketing Loan Assistance (MLB) programs in the 2008 Farm Bill.

With respect to relative efficiency, the same research notes that "providing price and yield compensation separately means that producers may receive support when they do not need it, or not receive support when they need it most. For example, a farmer who suffers a complete yield loss will not receive a payment under a price-based program that is tied to current production, (i.e., the MLB)."[2] Revenue and traditional programs are compared by simulating two revenue programs and the traditional programs over the 1975 to 2005 period and adjusting program parameters such that the average total costs are about equal ($3 billion per year). Using a coefficient of variation[3] to compare the two revenue programs with the traditional programs, revenue variation in the revenue programs was about half that of the traditional programs (Appendix Table 1).[4] The simulation results in Table 1, and also illustrated in Appendix Figure 1, show the high and low payments are less frequent in the revenue based program, with the revenue programs payments between about 50% below to 60% above the average payment within a 90% confidence interval. This compares to the traditional program variation 90% confidence interval of almost 90% below to nearly 130% above the average payment.

In establishing an area or farm level revenue program, there are two issues to consider. First, setting revenue per acre at the Crop Reporting District (CRD) level affords greater statistical reliability. It is clearly more robust than the county level given the gaps in adequate yield data across the country. Cooper (2009) cites "county-level production data is not reported by NASS in cases where either the county has no acreage planted to the commodity or the sample size of farmers is deemed too low to report he county data. In our analysis, for estimating the county-level yields, missing data points are substituted by crop district estimates."[5]

USDA Research in 2011 on adjusting the ACRE Program from a state level to national, crop district or county levels notes "experience with county-level yield and revenue insurance and the Federal crop insurance program illustrates the data challenges with a county-crop program. In 2009 and 2010, RMA deleted about a third of the county revenue and yield insurance programs, Group Risk Plan and Group Risk Income Protection, for corn, soybeans, grain sorghum, cotton, and peanuts (USDA, Risk management Agency, 2009). While most of these counties had little

[2]Ibid. p. 12.
[3] A measure of dispersion around a mean value of a distribution thatis calculated by dividing the mean by the standard deviation of the distribution.
[4]Cooper, 2009. op. cit. p. 12.
[5]Ibid. p. 35.

or no participation in GRP or GRIP, NASS' ability to produce estimates for counties outside the major growing areas was uncertain."[6]

Second, for a limited budget environment, the area level for payment determination is the optimum for delivering assistance when the producer needs it the most. The 2011 USDA ACRE analysis examines the relationship of reducing the level of statistical aggregation from state to CRD to county to farm in Appendix Table 2[7]. As shown, farm level variability ranges from about 140% of district CRD level to 320%. In Table 3[8], differences in average expected payment are shown, relative to a state-triggered program at different levels of aggregation, when the expected marketing year price is held equal to the revenue guarantee price. Payments increase by about 80% to 128% when the payment determination level is changed from the district to the county level.[9] Nevertheless, NCGA recognizes that some members of the Committee will find a county-level payment determination more attractive.

These two tables suggest that a further lowering of payment determination to the farm level would further increase costs. With a limited budget, the increase in payments at each level must be accompanied by a reduction in the amount of that payment that may be made on each acre so that the total expenditure does not increase. Table 2 indicates that reduced payments would be made two to three times as frequently at the farm level as at the CRD level. That suggests that growers would receive the same total amount of payments, but more frequently and in smaller amounts and that they would be more related to farm yield variability than to price variability. The current crop insurance program already provides the means to manage this type of risk. Moreover, this trade-off, from greater payments at the CRD to lower payments at the farm, means that sudden and prolonged price downturns of the type that occurred from 1998 to 2001 would result in payments being reduced from the 85% payment factor in the ARRM program to perhaps half of that amount. A second trade-off relates to land rents. Less variable, more frequent producer payments are more readily capitalized into land values and rents. As we have seen with direct payments, this does little to reduce the producer's operating risk.

There are two exceptions to these arguments for CRD payment determination. First are those producers whose farm revenue correlation with the area is sufficiently low that even though an area program might provide adequate assistance over time, it would not reliably occur when the producer needed it on the farm. Second are producers, who because of premium expense, purchase individual levels of crop insurance coverage below the 75 percent level to which some proposed revenue programs extend, including ARRM. This gap in coverage between ARRM, the farm program and individual crop insurance coverage has been referred to as the "doughnut hole". NCGA offers two suggestions to address these types of circumstances.

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[6]Dismukes,R., K. H. Coble, D. Ubilav, J. Cooper, and C. Arriola. 2011. *Alternatives to a State-Based ACRE Program: Expected Payments Under a National, Crop District, or County Base*, ERR-126, U.S. Department of Agriculture, Economic Research Service, September.p. 25.

[7]Ibid. p.2.

[8]Ibid. p. 5.

[9] These proportional changes in payments are constant as the value of the payments change with the guarantee price. Ibid. p. 5.

Indifference adjustment factor

Provide farm level revenue determination to those growers with low correlation between farm and CRD; we do not specify what this level of low correlation should be. Because farm-level revenue variability is greater than area level variability, a farm level ARRM would provide more payments to a producer than an area level determination. NCGA proposes an adjustment to the farm level payment such that a producer would be indifferent between farm and area level payment determination based total expected benefits from the program. An indifference adjustment factor would be calculated such that the producer would receive an equal amount of expected value at the farm as at the area, CRD or county. Note that a farm-level determination would remove the need for a farm-level qualifying loss that the CRD-level payment would require.

Gap coverage option

Like other plans, such as Supplemental Coverage Option or Total Coverage Option, this would allow a producer to buy area coverage, likely at the county level in a GRIP or GRP policy, at coverage up to 75% and extend to the coverage of the individual insurance policy, as low as 50%. The higher the level of individual coverage is, the lower the premium on the gap coverage. The gap coverage premium would effectively be the difference between the area 75% premium and the area premium calculated for the individual coverage, extending from 75% to 50%. The area premium could have an increased subsidy over that currently provided in the crop insurance statute, but NCGA does not specify one at this time.

Farm examples

To illustrate how ARRM might work with an indifference adjustment factor for a farm-level ARRM and a gap coverage policy, three examples of corn operations are provided in Appendix Table 4. These examples lie in the heart of, on the periphery of, and well beyond the Corn Belt in McLean County Illinois, Valley County Nebraska and Weld County Colorado, respectively. All calculations are based on a $4.50 average expected price and expected yields. The calculation of gap coverage assumes an individual insurance policy at 65% coverage and the total premium equals the difference between a GRIP 75% coverage policy and a 65% coverage policy based on the county's expected revenue. The producer premium is based on the current statutory subsidy of 55% for 65% coverage, although, as stated before, an increased subsidy is possible, but not specified.

ARRM expected payments for McLean County are $18.16 per acre at the CRD level; at the farm-level the payment would be identical because the indifference adjustment factor of .538 would make them equal. The calculation of gap coverage premium is based on expected revenue of $808 per acre; total and subsided premium for the 75%-65% coverage band would be $5.02 and $2.26 per acre, respectively.

In the Valley County example, expected CRD-level and farm-level payments are $12.75 per acre and the indifference adjustment factor that would equate them is .505. Gap coverage is based on

expected revenue of $767 per acre; total and subsided premium for the 75%-65% coverage band would be $4.04 and $1.82 per acre, respectively.

Finally, the Weld County farm would receive expected CRD-level and farm-level payments are $7.31 per acre and the indifference adjustment factor that would equate them is .234. Gap coverage is based on expected revenue of $790 per acre; total and subsided premium for the 75%-65% coverage band would be $1.72 and $0.77 per acre, respectively.

There are certain things our federal government must do for its citizens and providing food security is one of them. Countries around the world understand the important role that agriculture plays in their economies. They, too, provide assistance to farmers when needed along with resources for long term strategic investments in research and other priority programs. The 2012 Farm Bill presents an opportunity to advance needed improvements in the commodity title that can work more effectively with a strong federal crop insurance program. NCGA appreciates the difficult task before your Committee to write a comprehensive and balanced farm bill, especially under the current budget constraints. I thank for your time today and your consideration of our policy recommendations

APPENDIX

Table 1[10]

Stochastic analysis of the distribution of corn program payments under alternative U.S. programs (2005 expected prices and yields)

	Payment type			
Target Revenue Program	Total	Extended Coverage	Production Limited	Basic[1]
Mean payment ($ billion)	3.03	1.16	1.64	0.22
Coefficient of variation[2]	0.32	0.52	0.24	1.06
90% confidence interval (lower, upper)	1.62, 4.80	0.39, 2.28	1.06, 2.37	0.02, 0.73
Market Revenue Program	**Total**	**National[3]**	**Supplmental**	
Mean payment ($ billion)	3.17	2.33	0.85	
Coefficient of variation	0.34	0.430	0.59	
90% Confidence interval	1.55, 5.09	0.76, 4.06	0.37, 1.97	
Traditional-Style Program	**Total**	**P-MLB**	**P-CCP**	**Disaster**
Mean payment ($ billion)	3.11	1.26	1.67	0.19
Coefficient of variation	0.68	1.35	0.53	1.46
90% confidence interval	0.38, 7.10	0.00, 4.78	0.00, 2.28	0.02, 0.83

[1]The "basic" payment covers shortfalls in county revenue per acre with respect to expected county revenue per acre. The "extended coverage" payment is based on a target revenue using a statutory price, and provides supplemental coverage over the basic payment. The "production-limited" payment is similar to the extended coverage payment but applied to a fixed base acreage for the farmer, and provides supplemental coverage over the extended coverage payment.

[2]The coefficient of variation in this application is a measure of the dispersion of the probability distribution of revenue per acre that allows comparisons across populations with different means, and is the standard deviation of revenue per acre divided by the mean revenue per acre. The smaller the coefficient of variation, the lower the dispersion relative to the mean value of the distribution.

[3]The "national" revenue payment rate is based on the difference between national expected and actual revenue per acre, and the "supplemental" revenue payment provides additional coverage based on a county- level payment rate.

[10] Cooper. 2009. op. cit. p. 13.

Figure 1[11]

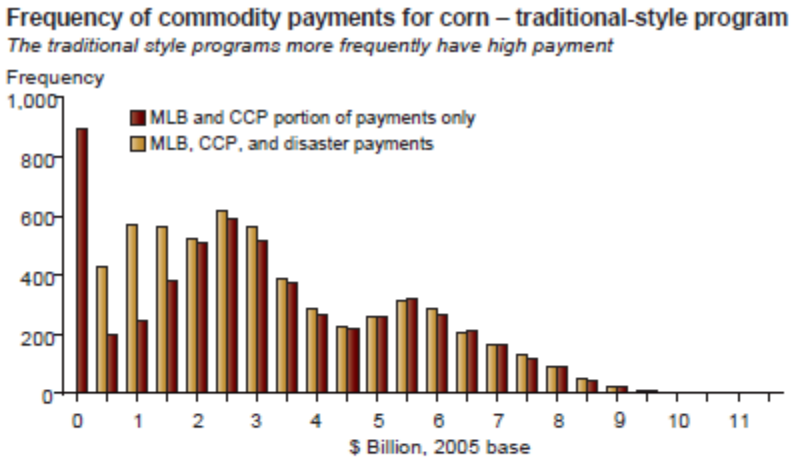


Figure 5b

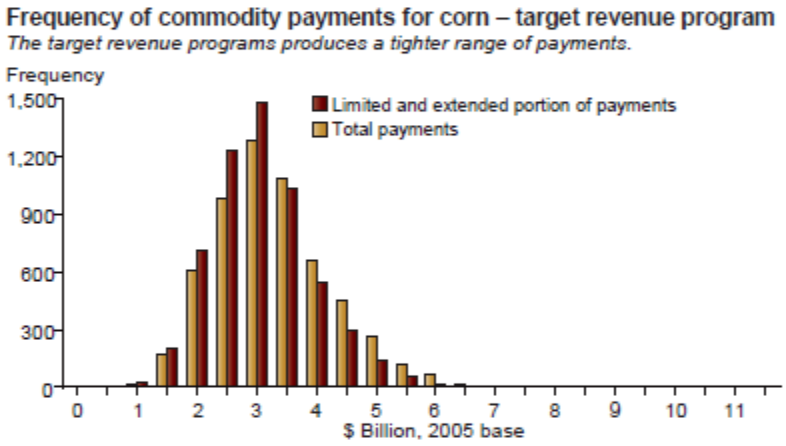
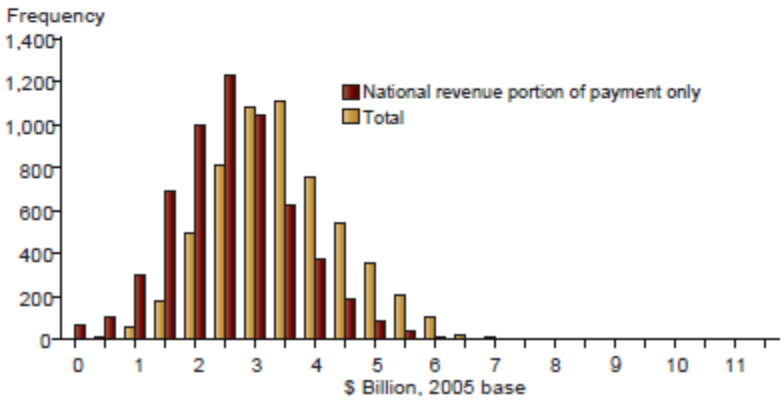


Figure 5c



Note: Each bar covers a $500 million range of payments. The taller the bar, the greater the number of payments falling in the associated range.

[11]Ibid. p. 15.

Table 2[12]

Yield and revenue variability at different levels of aggregation

Item/Level	Corn	Soybeans	Wheat	Cotton	Grain sorghum	Rice, long-grain	Rice, Medium/short-grain
	Coefficient of Variation						
Yield variability:							
National	0.069	0.058	0.056	0.076	0.099	0.037	0.061
State	0.097	0.099	0.135	0.119	0.123	0.043	0.061
District	0.110	0.113	0.169	0.152	0.167	0.045	0.062
County	0.122	0.125	0.195	0.184	0.202	0.052	0.067
Farm	0.359	0.372	0.520	0.672	0.776	0.335	0.263
Revenue variability:							
National	0.195	0.188	0.185	0.197	0.214	0.272	0.288
State	0.207	0.205	0.215	0.225	0.230	0.275	0.288
District	0.214	0.213	0.240	0.250	0.256	0.275	0.288
County	0.221	0.220	0.261	0.274	0.283	0.276	0.289
Farm	0.413	0.425	0.558	0.715	0.829	0.440	0.395

Averages weighted by acres harvested in 2010. District = Crop Reporting District. Medium/short-grain rice is for a single State, California. Based on simulations.

Table 3[13]

Difference in average expected payment, relative to State-triggered program, from revenue programs triggered at different levels of aggregation

Level	Corn	Soybeans	Wheat	Cotton	Grain sorghum	Rice, long-grain	Rice, medium/ short-grain
	Percent						
National	-11.3	-8.4	-11.5	-23.3	-10.1	-2.1	0
District	10.4	6.8	15.3	13.1	17.1	Less than 1	Less than 1
County	18.8	15.5	28.0	28.5	32.0	2.3	Less than 1

Averages weighted by acres harvested in 2010. District = Crop Reporting District. Medium/short-grain rice is for a single State, California. Based on simulations of expected market price equal to revenue program guarantee price.

[12]Dismukes et al. 2011. op. cit. p. 2.
[13]Ibid. p. 5.

Table 4

Expected Payments for ARRM with Adaptations for Corn in Selected Counties, 2010 Expect Revenue, Corn Expected Price = $4.50			
	McLean IL	**Valley NE**	**Weld CO**
Program	**$ per acre**		
ARRM-CRD	18.16	12.75	7.31
ARRM-Farm	18.16	12.75	7.31
Indifference adjustment	0.538	0.505	0.234
Gap Coverage			
GRIP Expected Revenue	$808	$767	$790
Total premium	5.02	4.04	1.72
Producer Premium	2.26	1.82	0.77

REFERENCES

Cooper, J. 2009. *Economic Aspects of Revenue-Based Commodity Support*, ERR-72, U.S. Department of Agriculture, Economic Research Service, April.

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HEADQUARTER OFFICE
632 Cepi Drive
Chesterfield, Missouri63005
(636) 733-9004
FAX: (636) 733-9005

WASHINGTON DC OFFICE
122 C Street NW, Suite 510
Washington, DC20001-2109
(202) 628-7001
FAX: (202) 628-1933