Testimony of

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Committee on Agriculture
Subcommittee on General Farm Commodities and Risk Management

Formulation of the 2012 Farm Bill: Commodity Programs & Crop Insurance

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Introduction

Chairman Conaway, Ranking Member Boswell, and Members of the Subcommittee, thank you for the opportunity to offer testimony on how commodity programs will affect producers in the 2012 Farm Bill.

My name is Linda Raun. My husband LG and I raise 1000 acres of rice in Wharton County near El Campo, Texas. We have been actively farming since 1976. I currently serve as chairwoman of the USA Rice Producers' Group and I also serve on the College of Agriculture Development Council at Texas A&M University. I have previously served as a Lower Colorado River Authority Director and served two terms on the Texas State Committee for the Farm Service Agency. My testimony here today is on behalf both the USA Rice Federation and the US Rice Producers Association.

U.S. Rice Industry Overview

The U.S. rice industry contributes $34 billion in economic activity and provides jobs and income for not only producers and processors of rice, but for all involved in the value chain, contributing to 128,000 jobs. Much of this economic activity occurs in the rural areas of the Sacramento Valley in California, the Mississippi Delta region including Arkansas, Mississippi, and Missouri and in my home area, the Gulf Coast region of Texas and Louisiana.

The U.S. rice industry is unique in its ability to produce all types of rice, from long grain, medium grain, and short grain, to aromatic and specialty varieties. Last year, U.S. farmers produced a rice crop of nearly $3 billion as measured in farm gate value.

Today, about 86 percent of all the rice that is consumed in the U.S. is produced here at home. And, despite significant trade barriers to exports, the U.S. remains the largest non-Asian exporter of rice and the third largest exporter worldwide. On average, between 40 to 50 percent of the annual rice crop is exported as either rough or milled rice. The top U.S. export markets for rice include Mexico, Japan, Canada, and Haiti. In 2011 we exported over $2 billion in rice to markets around the world.

Beyond the substantial economic benefits of rice is the environmental dividend from winter-flooded rice fields that provide critical habitat for migratory waterfowl and other wetland-dependant species. All of the major rice-production areas in the U.S. host important waterfowl activity during winter months. Rice-growing areas provide surrogate habitats for hundreds of wildlife species that rely on wetland conditions for species survival, some of which would be threatened but for the wetland environments provided by flooded rice fields.

Without rice farming, wetland habitats in the U.S. would be vastly reduced. Maintaining U.S. rice acres provides conservation benefits of national significance that are vitally important because annually, anywhere from 2.5 to 3.0 million U.S. rice acres are an irreplaceable and invaluable conservation safety net for migratory waterfowl such as ducks and geese.

In my home state of Texas, we are concerned with the lasting effects of the drought conditions in 2011. Because of a decision by the Lower Colorado River Authority to reserve back a portion of the water that would have been sold to farmers for use in their rice fields, Texas will lose one third of their rice acres for the 2012 crop year. The increased demand for water between consumers, agriculture, and other industries further emphasizes the need for strong farm policy in this country.

Importance of Agriculture and Cost-Effective Farm Policy

The U.S. agriculture sector is one of the few bright spots in the U.S. economy. In a time of economic downturn, agriculture producers have managed to remain profitable, create new jobs, and continue to provide consumers in the U.S. and all over the world with a safe and abundant supply of food and fiber. U.S. agriculture is vitally important to America and an effective farm policy safety net is critically important to U.S. agriculture.

Following the recent passage of the Agriculture Reform, Food, and Jobs Act of 2012 by the Senate Agriculture Committee, the rice industry remains concerned that the policy needs of many crops in many regions of the country were largely ignored in that bill. As you know, farm bills tend to have regional differences due to the needs of different crops grown in diverse regions. However, historically farm bills have been developed that took into account these differences and provided a workable policy for all crops and regions. We are discouraged to see a change in this practice as regards the Senate Agriculture Committee bill. All regions of the country experience risk in crop production. Therefore, one appropriate manner to judge effectiveness is to consider the amount of risk protection provided in the form of dollars spent. This is especially true when a farm bill involves new programs whose effectiveness is untested. Necessary mid-course adjustments are not inconceivable in this scenario. Estimates show that Midwestern and Northern farmers will have an increasingly disproportionate share of the baseline and Sunbelt crops will be left with a further shrinking baseline coupled with ineffective risk protection for many crops. ***(See Chart 1)***

With the House and Senate farm policy recommendations to the Joint Committee on Deficit last fall, Agriculture became the only industry to offer reductions in spending for the purposes of debt reduction. While farmers have always been willing to do their part for deficit reduction, I would urge lawmakers to reject cuts to U.S. farm policy that would exceed the levels recommended in the proposal that the House and Senate Agriculture Committee Chairs and Ranking Members had agreed to.

I firmly believe that any cuts must also focus on areas of the budget outside of farm policy that have not yet contributed to deficit reduction yet comprise a significant share of the federal budget and the farm bill baseline.

2008 Farm Bill Review

The 2008 Farm Bill continued the non-recourse marketing loan, loan deficiency payment, and the direct and counter cyclical payment policies. While the counter-cyclical payment and marketing loan have been helpful in the past, they have recently been overwhelmed by the cost of production. If crop prices drop sharply producers will be in dire financial straits by the time these policies make payments. The direct payment, whatever its imperfections, has assisted rice producers in meeting the ongoing and serious price

risk of farming in today's environment. We have come to understand and accept the political reality that direct payments will be eliminated, even though the Federal government has long been consistently sending signals to the agriculture community that we should shift our policies towards those that are green box and WTO friendly. It is a bit ironic that the rice industry heeded those instructions in previous farm bills, and we, more than any other commodity, will be severely impacted by the loss of the direct payment unless Congress works with us to find a workable policy solution.

The new policies created in the 2008 farm bill included the addition of Average Crop Revenue Election (ACRE) as an alternative to counter cyclical payments for producers who agree to a reduction in direct payments and marketing loan benefits. The bill also added Supplemental Revenue Assurance (SURE) as a standing disaster assistance supplement to federal crop insurance.

Neither the ACRE nor the SURE policy has offered much value to rice farmers. Specifically, in the first year of ACRE signup, only 8 rice farms representing less than 900 acres were enrolled nationwide. And SURE has provided little, if any, assistance to rice producers, including those producers in the Mid South who suffered significant monetary losses in 2009 due to heavy rains and flooding occurring prior to and during harvest, or the significant losses last year as a result of spring flooding in the Mid South. SURE's inability to provide disaster assistance for such catastrophic events further highlights the continuing gap in available programs to help rice producers manage or alleviate their risk.

The 2008 Farm Bill also made substantial changes to the payment eligibility provisions, establishing an aggressive adjusted gross income (AGI) means test and, albeit unintended by Congress, a very significant tightening of "actively engaged" requirements for eligibility. USDA was still in the process of implementing many of the provisions of the 2008 Farm Bill in 2010, and the final payment eligibility rules were only announced in January of that same year, a mere two years ago. Consequently, we are still adjusting to the many changes contained in the current farm bill, even as Congress writes the 2012 farm bill.

2012 Farm Bill

With the above mentioned as a backdrop, the U.S. rice industry developed a set of farm policy priorities in September of last year to guide us during consideration of the 2012 Farm Bill. The U.S. rice industry is unified in its firm belief that farm policy designed to support a strong and dynamic U.S. agriculture sector is absolutely vital. Although the different growing regions within our industry are interested in utilizing policy options in different ways, we remain united and committed to effective farm policy for all growing regions for all crops. Any rumors regarding a split in the rice industry or a difference of preferred policy for rice producers is inaccurate. We support a choice for rice producers because we recognize that a one-size-fits-all policy will not result in an effective risk management policy for all regions.

The development of farm policy should be focused on providing producers with price protection, not just for price moves during the growing year, but for multiple years of price declines as we saw occur in the late 1990's. Those that hold out crop insurance as the centerpiece of farm policy certainly don't understand the nature of farming in my area. Crop insurance can't, and it was not designed to, provide price protection across multiple years. Adequate price protection is the most critical component of the next farm bill and must be included in any policy option.

Right now prices are decent for many crops, but we all know how cyclical commodity prices are, and every grower needs a policy that will provide some downside price protection if (and likely when) we see a steep decline in commodity prices. Without this type of certainty, farmers, like any businessperson, will take steps to minimize their exposure to risk, resulting in a pullback in investments for their farm. This

pullback starts first with their suppliers of inputs (equipment, grain storage facilities, fertilizer) and then begins to impact the majority of businesses in rural America. We've seen this cycle play out over and over and I hope we will not repeat the mistakes of the past by putting in place a farm policy that assumes good prices are here to stay, and then we find out it is ill-equipped to deal with the decline in prices that is sure to come. ***(See Chart 2)***

Effective farm policy gives producers the confidence we need to continue to invest in our farms and the confidence that lenders need to extend the financing to producers to make these investments.

I hear some contend that a revenue-based policy with no reference or floor price is the right approach to take in this farm bill and is all that is needed when coupled with crop insurance. It seems to me that this approach is flawed in several ways. First, this assumes that crop insurance works equally well for all crops and regions, which I can assure you is not the case today. Second, this assumes that we won't face another 1998 through 2002 scenario where we had good commodity prices that quickly fell to catastrophic levels due to global factors. Third, this assumes that if commodity prices fall then input costs will decline in sync and proportional to the decline in prices. I have to say that if history is any guide, then I believe all three of these assumptions will prove wrong. And by not planning now for this type of scenario, we are setting ourselves up for another situation where farm policy will not be equipped to respond to this price decline. The result will be a significant economic downturn in rural America, followed by calls for Congress to provide additional economic assistance in a time of large Federal budget deficits and debt.

In addition, what happens if the price of only one or two commodities decline sharply? I can't imagine that input costs are going to decline in this scenario, so producers of these crops are forced to deal with a severely depressed price environment where our options are to either stop producing all together, or shift into the other crops with higher prices. This could have severe implications to the infrastructure for the crops with depressed prices and reduced production. We have seen this occur in some areas with rice infrastructure and I believe we can ill-afford a farm policy that would not provide us with effective down side price protection to forestall any further contraction of this industry.

Given the budget pressures and other considerations facing Congress that have caused policymakers to consider altering the former policies in favor of more directed and conditioned assistance, we developed the following priorities:

- First, we believe the triggering mechanism for assistance should be updated to provide tailored and reliable help should commodity prices decline below today's production costs, and should include a floor or reference price to protect in multi-year low price scenarios.
- Second, as payments would only be made in loss situations, payment limits and means tests for producers should be eliminated, or at a minimum, not further tightened.
- Third, federal crop insurance should be improved to provide more effective risk management for rice in all production regions, beginning with the policy development process.

More specifically relative to each of these points, we believe that:

Price Protection is a Must

Given price volatility for rice is the primary risk producers face and they do not have an effective means of protecting themselves against such price volatility, with price fluctuations largely driven by global supply and demand; given rice is one of the most protected and sensitive global commodities in trade negotiations, thus limiting access to a number of key markets (indeed we were excluded in the South

Korea FTA); given costs of production have risen to a point where the current $6.50 (loan rate)/$10.50 (target price) assistance triggers are largely irrelevant, we believe the first priority should be to concentrate on increasing the prices or revenue levels at which farm policy would trigger so that it is actually meaningful to producers, and would reliably trigger should prices decline sharply. ***(See Chart 3)***

The reference price for rice should be increased to $13.98/cwt ($6.30/bu). This level would more closely reflect the significant increases in production costs for rice. Ideally, this minimum could move upward over time should production costs also increase, this being of particular concern in the current regulatory environment. And this reference price should be a component of both a price-loss policy option and a revenue-loss policy option to ensure downside price protection.

The existing price trigger levels have simply not kept pace with the significant increases in production costs. It is for this reason that I believe strengthening U.S. farm policy would be helpful in ensuring that producers have the ability to adequately manage their risks and access needed credit.

Options for Different Production Regions

We recognize that a one-size-fits-all approach to farm policy does not work effectively for all crops or even the same crop such as rice in different production regions. Using rice as an example, this is a crop grown in a fairly limited geographic area, yet there are distinctions between growing regions that make a difference in what policy will work best for rice.

In the Mid-south and Gulf Coast production regions, a price-based loss policy is viewed as being most effective in meeting the risk management needs of producers. Specifically, this policy should include a price protection level that is more relevant to current cost of production; paid on planted acres or percentage of planted acres; paid on more current yields; and take into account the lack of effective crop insurance policies for rice.

In the California production region, although the existing ACRE policy still does not provide effective risk management, efforts to analyze modifications which will increase its effectiveness continue. Since rice yields are highly correlated between the farm, county, crop reporting district, and state levels, we believe that a revenue plan should be administered for rice at either the county or crop reporting district level to reflect this situation rather than lowering guarantee levels to use farm level yields. Due to a host of differences in market prices, production costs, yields, marketing patterns, and uses, there is the potential for a properly designed revenue-based policy to work for rice growers in California, while I know that for my rice enterprise in Texas I need a price-based policy. Every crop has very different pricing and marketing options.

While I have focused on the need for a choice for rice producers in different regions, this also applies for producers of most other grains. I support having policy options available for all crops, and believe that both a price-based policy and a revenue-based policy should be offered as options.

My husband and I are not fortunate to farm in an area where we have the ability to rotate among several crops. Some production regions have that ability, but some do not and may be limited to just one or two crops that can be profitably produced. Because of this great diversity across American agriculture we need policy options that I can use to tailor the best risk management tools possible on my farm.

Future policies should be plain and bankable. The current ACRE program, while offering improved revenue-based protection, is complicated by requiring two loss triggers; providing payments nearly two years after a loss; and provides no minimum price protection — it is not bankable. The marketing loan

and target prices are plain and bankable — unfortunately the trigger prices are no longer relevant to current costs and prices.

Farm policy must be defendable. We believe it makes sense to provide assistance when factors beyond the producer's control create losses for producers. We generally think more tailored farm policies are more defendable. For this reason, we like the thought of updating bases and yields or applying farm policies to planted acres/current production and their triggering based on prices or revenue, depending on the option a producer chooses. However, policy choices should not result in severe regional distortions in commodity policy budget baselines from which reauthorized commodity policies must be developed. In addition, care must be taken in order to ensure that producers who have utilized the flexibility of past farm bills are not disadvantaged in the construct of updating bases. We are particularly concerned with the effect this may have on small producers from the preliminary and incomplete data that we have seen.

Protection to withstand a multi-year low price scenario. Whether in a revenue-based plan, or a price-based plan, reference prices should protect producer income in a relevant way in the event of a series of low price years. Ideally, this minimum could move upward over time should production costs also increase, this being of particular concern in the current regulatory environment.

Whatever is done should not dictate or distort planting decisions. Direct payments were excellent in this regard. SURE or similar whole farm aggregations tend to discourage diversification, which could be a problem for crops like rice. Any commodity specific farm policy that is tied to planted acres must be designed with extreme care so as to not create payment scenarios that incentivize farmers to plant for a farm policy. Whatever is done should accommodate history and economics and allow for proportional reductions to the baseline among commodities. Some commodities are currently more reliant on countercyclical farm policies (ACRE/CCP) while others are receiving only Direct Payments in the baseline. Generally, the least disruptive and fairest way to achieve savings across commodities would be to apply a percentage reduction to each commodity baseline and restructure any new policy within the reduced baseline amounts.

There have been concerns raised about higher reference prices distorting planting decisions and resulting in significant acreage shifts including for rice. We are unaware of any analysis that shows significant acreage shifts resulting from the reference price levels included in the 2011 Farm Bill package. In fact, for rice specifically, a reference price of $13.98/cwt that is paid on historic CCP payment yields and on 85% of planted acres results in a reference price level well below our average cost of production, so I find it hard to imagine why someone would plant simply due to this policy given these levels.

As I have followed the current farm bill debate since last fall, I am amazed at some of the assertions about a price-based policy distorting planting decisions and resulting in large acreage shifts. The price levels that I understand were developed last year and how they were factored based on acreage and yield percentages would have meant they were well below our costs of production for all crops. This idea that maintaining a price-based policy is somehow distorting, and that a revenue-based policy that is based off historically high prices is non-distorting is misleading. In addition, it is incredibly naïve and inaccurate to believe that only reference prices/target prices in a counter cyclical or similar policy have the ability to create planting distortions. Indeed, many of the planting shifts seen recently have resulted from pressures created by policies outside the farm bill – for example our energy policy. It is important to recognize that disproportionate regional distribution of farm programs benefits not only raise questions of equity, but also should be recognized as a portent for distortions in farm policy, particularly with regard to planting decisions. Commodities receiving a disproportionate share of benefits will entice producers to plant those crops.

Pay Limits/Eligibility Tests Should Be Eliminated

I strongly oppose any further reduction in the payment limit and adjusted gross income (AGI) levels provided under the current farm bill. One can understand the desire to limit former policies such as the direct payment policy. However, the disadvantages of payment limits must be acknowledged in the construct of any farm policy, particularly a counter-cyclical policy. Payment limits have the negative effect of penalizing viable commercial size, family farms the most when crop prices are the lowest and support is the most critical. To be a viable farm, we must use economies of scale to justify the large capital investment costs associated with farming today. It is essential that producers maintain eligibility for all production to the non-recourse loan. Arbitrarily limiting payments results in farm sizes too small to be economically viable, particularly for rice, cotton, and grain farms across the Sunbelt. The current payment limit and AGI provisions have created significant paperwork burdens and costs to producers to comply and remain in compliance. This is particularly true for family farms that have reorganized not to take advantage of any payment limit concerns, but to protect themselves against estate tax liability. As oppressive as the current limits are, at a minimum Congress should not make any further reductions or limits that further penalize commercially viable farms.

Farm policy should not be limited based on arbitrary dollar limits. Assistance should be tailored to the size of loss. A producer should not be precluded from participating in a farm policy because of past income experience. The Senate Agriculture Committee Farm Bill AGI test of $750,000 is an extraordinary reduction from current policy and can have a significant impact, particularly on tenant farmers who may be forced into cash rent situations due to the ineligibility of the landowner due to the further restrictive AGI rule.

The actively engaged payment eligibility requirements included Senate Agriculture Committee Farm Bill would tighten these rules even further to the point that individuals responsible for very vital functions in the farm, i.e. marketing, could be deemed ineligible for farm policy. They contain the promise of a future mired in even more paperwork and accounting nightmares. They appear to be reforms foisted on unsuspecting producers by a leadership disconnected with the realities of everyday farming all in the name of program compliance. We would ask that you remember that many of these changes affect every single producer, not just those who may be in danger of approaching arbitrary payment limits or eligibility requirements. While we are still examining the effects of the changes, these highly technical proposals appear to change even the spousal eligibility rule. In short, we remain strongly concerned that the eligibility requirements and means tests would attempt to eliminate the way farms conduct their business.

Crop Insurance Should Be Improved

Risk management products offered under Federal Crop Insurance have been of very limited value to rice producers to date due to a number of factors, but primarily because the risks associated with rice production are unique from the risks of producing many other major crops. Indeed, it is quite ironic that the Senate in developing its crop insurance provisions recognizes the need to distinguish between irrigated and non-irrigated crops by having specific provisions to address the inequities that result in irrigated situations. Unfortunately, this recognition did not extend to their commodity policy proposal where they demand a one-size-fits-all policy.

For example, since rice is a flood-irrigated crop, drought conditions rarely result in significant yield losses as growers simply pump additional irrigation water to maintain moisture levels to achieve relatively stable yields. However, drought conditions do result in very substantial production cost increases as a result of pumping additional water.

Rice has traditionally been underserved by crop insurance and that is still largely the case today. ***(See Chart 4)*** As a result, we have on average lower coverage levels and, in some cases, higher premium costs for rice.

I think it is inappropriate to believe that crop insurance can ever be the sole policy producers rely on for risk management. Crop insurance is designed to cover production shortfalls or price declines in a single year. It is not designed to protect against price declines over multiple years. And I find myself asking the question, and let me be clear I hope we don't see this happen, but if crop prices decline again in a scenario like we saw in the late 1990's how effective is crop insurance going to be then? If prices drop to those levels again it is clear that a crop insurance revenue policy is not going to be of much help to me as a producer with prices at these levels.

From a rice grower's perspective I have additional concerns about crop insurance. The risk management products offered under Federal Crop Insurance have been of very limited value due to a number of factors, including artificially depressed actual production history (APH) guarantees, which I understand is also a problem for many other producers; high premium costs for a relatively small insurance guarantee; a lack of convergence between the cash and futures prices for rice; and the fact that the risks associated with rice production are unique from the risks of producing many other major crops. What rice farmers like I need from federal crop insurance are products that will help protect against increased production and input costs, particularly for energy and energy-related inputs. For example, fuel, fertilizer, and other energy related inputs represent about 70 percent of total variable costs.

In this vein, many in the rice industry have been working for over the past four years now to develop a new generation of crop insurance product that might provide more meaningful risk management tools for rice producers in protecting against sharp, upward spikes in input costs. The objective was to gain approval from the Risk Management Agency (RMA) of at least two new products that could be available to growers in time for the 2012 crop year, but this has not materialized. We are still working on this effort, and hope to have a policy available for the 2013 crop. As with any new policy, there will be issues to work through so it is unrealistic to think rice can rely heavily on crop insurance for its risk management needs in the near future. But, it is important to stress that even if these products had become available this year, we do not believe that they would have put rice producers anywhere near on par with other crops in terms of the relevance that crop insurance has as a risk management tool.

To further reinforce this, the new Supplemental Coverage Option (SCO) crop insurance provision included in the Senate Farm Bill may hold some value for rice producers in better utilizing crop insurance. However, we are again hearing from RMA that due to data availability there is uncertainty as to how broadly this policy can be offered for rice, and even when it can be made available.

As such, rice producers enter the 2012 farm bill debate at a very serious disadvantage, having only a single farm policy that effectively works and that farm policy being singled out for elimination.

We also support improvement to the product development processes. In no case should the crop insurance tools, which are purchased by the producer, be encumbered with environmental/conservation regulation or other conditions that fall outside the scope of insurance.

Commodity Futures Market

Another risk management tool that is becoming more important for all producers is the use of the commodity futures market to hedge price risks for the crops produced. As we see the coming changes in

the farm bill, I think the ability to effectively use the futures market to price and market our crop will become imperative. Today growers have the ability to easily hedge corn, soybeans, and wheat, but with rice I am limited in the opportunity to hedge the crop due to issues with the rice futures contract. The contract has suffered from a lack of convergence between cash prices and the futures prices, and in some cases there has been a negative basis as wide as $4/cwt. While some of the price risk for other crops can be hedged, for the rice we grow, I am unable to do so on par with these other crops.

2011 Budget Control Act Efforts

Although the details of the 2011 Farm Bill package that was prepared by the House and Senate Agriculture Committees in response to the Budget Control Act were not fully disclosed, based on discussions and reports we believe that that package at least represents a good framework on which to build the 2012 Farm Bill. The 2011 package included a choice of risk management tools that producers can tailor to the risks on their own farms, providing under each of those options more meaningful price protection that is actually relevant to today's production costs and prices. It also included provisions to improve crop insurance and expedite product development for underserved crops such as rice.

The U.S. rice industry very much appreciates the Members and staff who put enormous time and effort into what we believe represents a good blue print for ongoing Farm Bill deliberations and we thank you.

Conclusion

Again, thank you for this opportunity to offer my testimony. We certainly look forward to working with you as the 2012 Farm Bill process moves forward. I would be happy to respond to any questions that you might have.

Chart 1

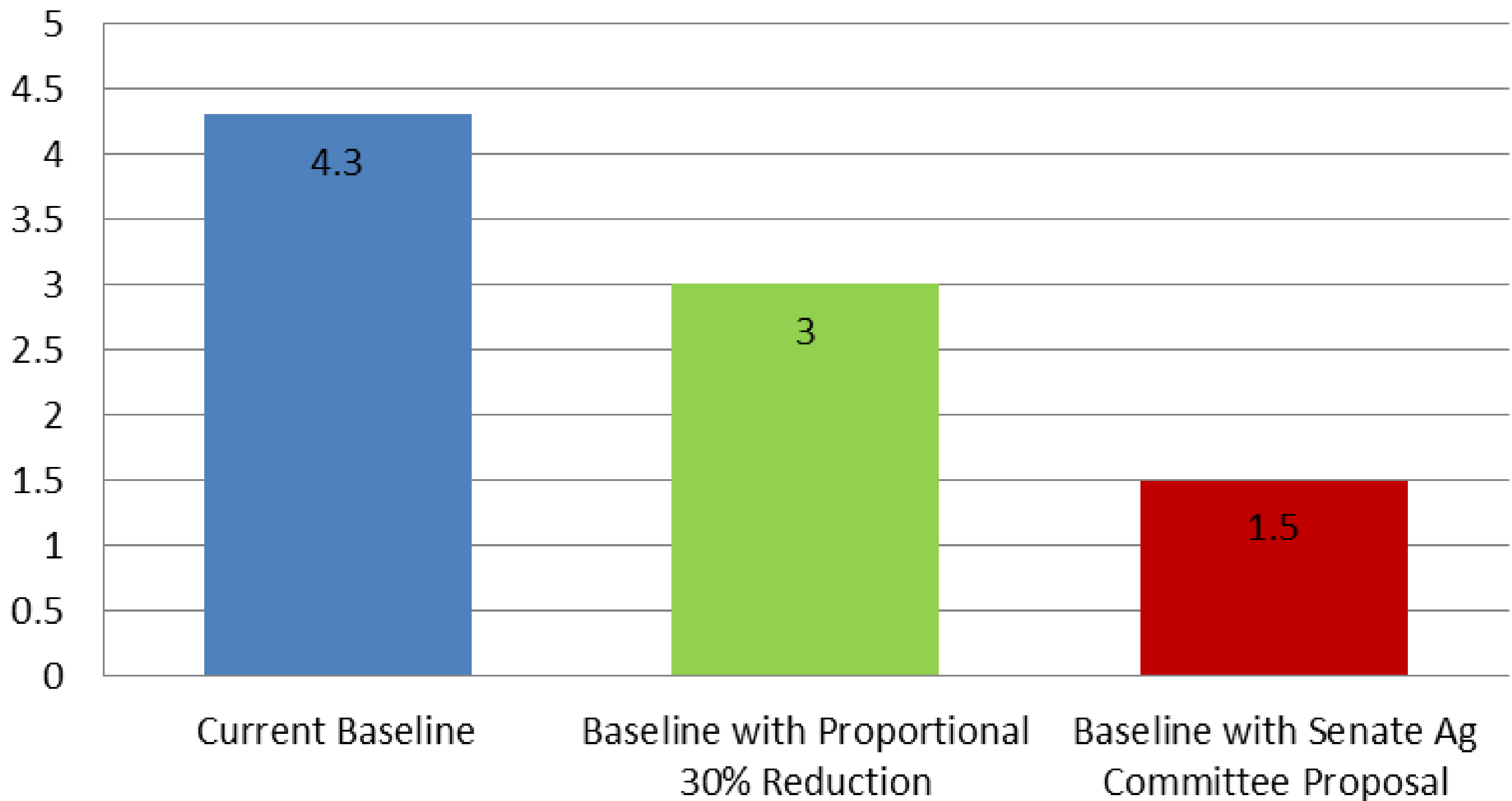

Chart 2 - Rice ARC Example

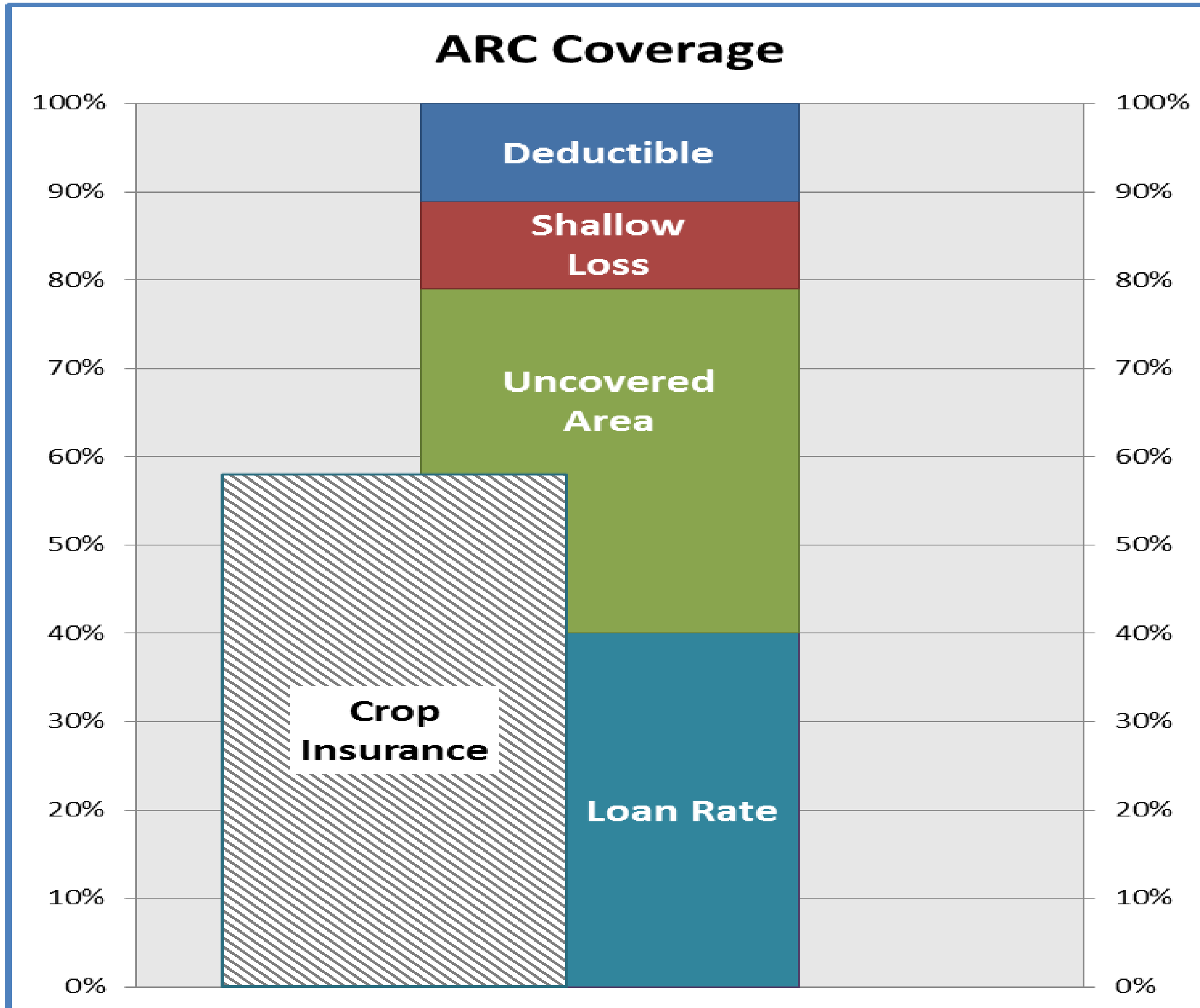

Chart 3 - Yield vs. Price Risk by Crop

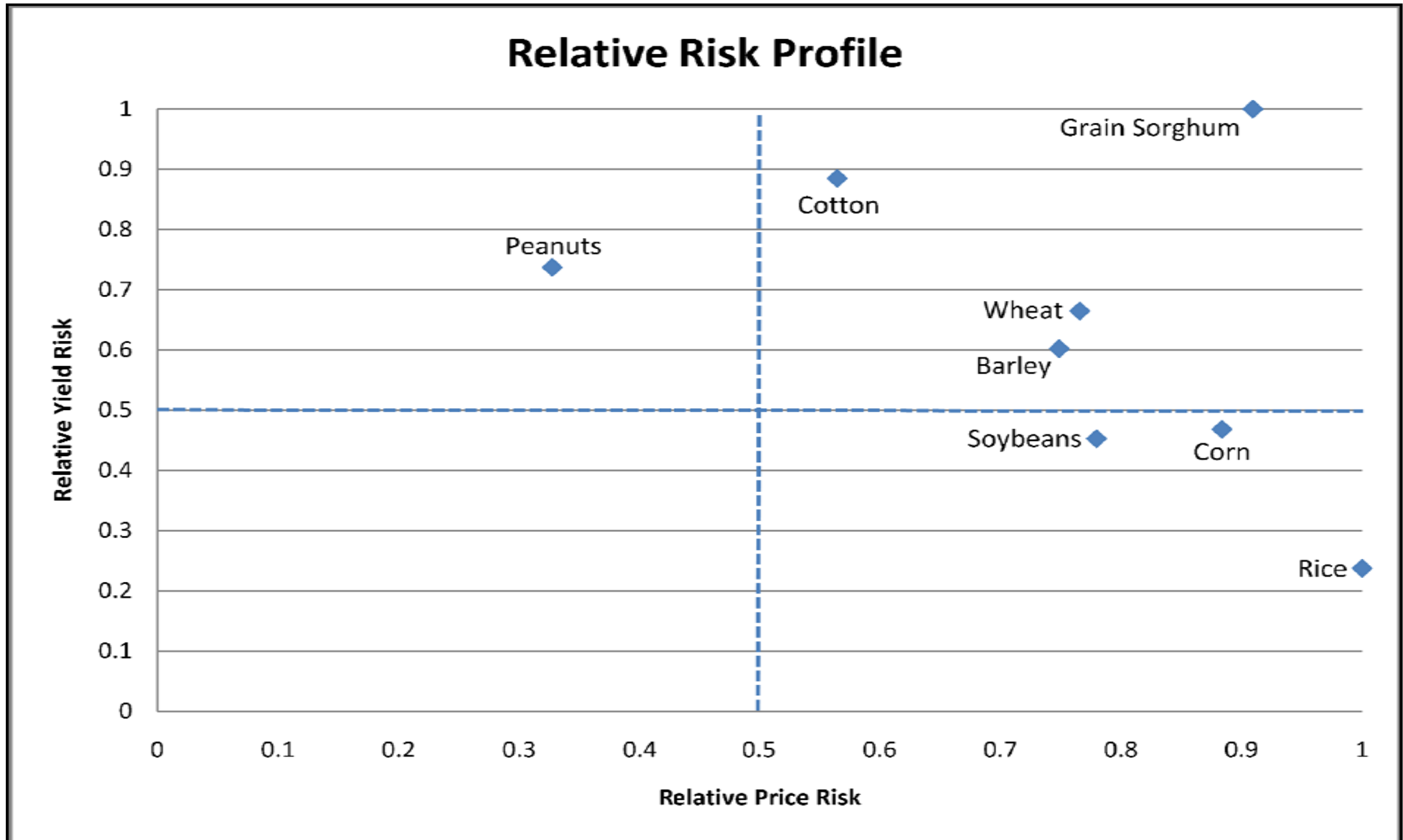

Chart 4