National Corn Growers Association
www.ncga.com

Testimony
Of
Anthony Bush
Chairman, Public Policy Action Team
National Corn Growers Association

Before the
U.S. House Agriculture Subcommittee on
General Farm Commodities and Risk Management

Longworth House Office Building
Room 1300
Washington, DC

June 24, 2010

Mr. Chairman, Ranking Member Moran and members of the Subcommittee, on behalf the National Corn Growers Association (NCGA), I appreciate the opportunity to share with you some perspectives on today's farm programs and their importance to our members' risk management planning.

My name is Anthony Bush. I am currently serving as the Chairman of NCGA's Public Policy Action Team. I am from Mt. Gilead, Ohio where my wife Teresa and I raise corn, soybeans and wheat on a fourth generation family farm.

The National Corn Growers Association represents more than 35,000 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.

Although it seems like just a short time ago that the 2008 Farm Bill's implementation was launched, NCGA recognizes the need for the House Agriculture Committee to begin planning for 2012 along with ensuring strong oversight over our current farm policies and programs. Knowing the extremely difficult fiscal and economic conditions that our nation must address today, NCGA has begun to prepare for policy discussions on improving the farm safety net and the various scenarios that could arise as a result of new budget realities confronting the Congress. In doing so, we look forward to making a strong case that for our growers to continue to meet the world's increasing demand for food, feed and renewable fuels, there will be need for even more effective risk management tools. In our view, the reforms adopted in the 2008 Farm Bill are serving to move the farm safety net in this direction.

HEADQUARTER OFFICE
632 Cepi Drive
Chesterfield, Missouri 63005
(636) 733-9004
FAX: (636) 733-9005

WASHINGTON DC OFFICE
122 C Street NW, Suite 510
Washington, DC 20001-2109
(202) 628-7001
FAX: (202) 628-1933

Over the past decade, U.S. corn growers have made significant progress in productivity in an increasingly competitive environment. Between 2000 and 2009, the national average yield has increased from 136.9 to 164.7 bushels per acre, over a twenty percent increase. In my home state of Ohio, we recorded a state wide average yield of 174 bushels per acre, an eighteen percent increase in yield. Although many growers in Ohio were hit hard in 2002 by drought conditions when the state average corn crop yield was 89 bushels per acre, the lowest average yield since then has been 135 bu/acre. Because of advances in seed technology along with modern production and conservation practices, the U.S. corn industry is well positioned to sustain a very positive yield trend. At the same time, though, this success is accompanied by a substantial increase in risk exposure, particularly market volatility.

From a low of $1.85 per bushel in 2000, the season average market price peaked at $4.20 in 2007, and has since declined to $3.50 last year, an increase of 90 percent. Since 2006, swings of more than $0.50 per bushel are common, causing dramatic fluctuations in gross revenue. Nationally, the average revenue per acre for corn increased almost 129 percent between 2000 and 2009. By expanding corn markets, especially a growing ethanol industry, the corn industry has certainly benefited from more robust commodity prices.

The same sources of demand growth for corn—rapid growth in developing economies, however, have also increased demand for farm production inputs; the result is a sharp rise in farmers' production costs. Over the past ten years, nitrogen and potassium fertilizer have jumped by an estimated 200 and 416 percent, respectively. Diesel fuel has increased by over 148 percent while biotech corn seed costs have risen by over 113 percent. Additionally, the average land rent per acre in the Corn Belt has increased 41 percent. Markets have determined that this recent increase in corn revenue is being mostly bid into the prices of inputs, rather than being mostly reflected in farm land values and rents. The effect is that, in spite of the attractive run-up in prices and yields, a significant amount of the implied wealth is flowing off the farm, leaving producer-landowners without a proportionately increased store of wealth in farm land that could be drawn upon to cushion revenue shocks in the future.

Farming is typically a capital-intense, thin-margin enterprise, but these higher production costs mean even more is at risk with the planting of a crop each year. In short, profit margins are still being squeezed requiring sound risk management plans and timely marketing of corn in order to adequately protect producers from significant crop losses as well as declining commodity prices. This is perspective of NCGA's comments on the development of the 2012 Farm Bill.

It is no surprise, then, that federal crop insurance's revenue based policies have become critically important to today's farm safety net. Just last year, the total liability protection for No. 2 yellow corn exceeded $31 billion for 503,670 policies, which sold for nearly $3.5 billion in total premium. Corn by itself represents around 40 percent of the aggregate premium.

Impressive as these numbers may be, NCGA remains very concerned with current policy premium levels in light of the fact that corn has experienced exceptionally low loss ratios under the existing rating system. Today's crop insurance program is required to operate with a national loss ratio of 1.0 with indemnities paid not to exceed total premiums. It is important to note the Federal Crop Insurance Act (FICA) provides for instructions to "ensure equity for producers" and to consider the relative performance for “commodities by area”. NCGA would argue that the program’s ultimate performance should be judged by equity for producers and that there should not be systematically differential performance by commodity, location, or by insurance product. While NCGA recognizes the complexity required to provide an actuarially sound rating system for the size and breadth of today’s crop insurance program, we believe an evaluation of the rating methodology’s historical performance should begin with a clear and complete documentation of actual results in the “real world”. Unfortunately, we were disappointed that the recent outside review of the Risk Management Agency’s rating system adopted a less comprehensive approach in its analysis.

If the current rating system was performing correctly, we would expect corn loss ratios to be randomly distributed around that of other crops. From 1990 through 2008, the loss ratio of corn only exceeded that for all other programs in 1993, one year out of the nineteen. In addition, loss ratio experience across crops and regions should converge over time if the rating system is performing as intended. However, NCGA sees little evidence of convergence. For example, the loss ratio from 1990 through 1999 averaged .91 for corn and 1.15 for all other programs, a difference of .24. From 2000 through 2009, the loss ratio was .67 for corn and .99 for all other programs, an even larger difference of .32. While today’s historical loss cost system may be designed to be self-correcting, the empirical facts suggest otherwise. Even though NCGA disagrees with the reviewers’ endorsement of the current system, we agree with a key recommendation for more appropriate weighting of early crop year observations and additional weather information for credible annual observations. Without significant changes to better reflect reduced yield variability, yield trend increases and appropriate weighting corrections, the rating system will continue to set premiums well above corn’s actual loss experience. Over the long term, more corn growers will not be able to adequately protect against significant revenue losses during a period of increasing market volatility and risk exposure.

To address gaps in protection against production shortfalls and volatile markets not adequately met by crop insurance, price based commodity programs and disaster aid, NCGA has advocated for a more market oriented revenue based risk management program. Revenue shortfalls are the direct cause of income reductions. Price declines do not necessarily result in reduced income since price declines have historically been accompanied by above average yields. The new Average Crop Revenue Election Program (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, yield trends and greater market volatility.

Unlike other farm programs, ACRE targets the risk that revenue for a crop year at the state level with a guarantee based on the previous two season average prices. ACRE is the only program that addresses multiple year revenue stability by limiting the movement of the guarantee to ten percent. Because crop insurance uses futures prices set during the cropping year, crop insurance does not protect against price changes across years. Similar to crop insurance, ACRE is limited to delivering assistance when an actual loss in crop specific revenue is sustained on the farm. Another distinct advantage of ACRE is that state and farm level benchmark revenues better reflect yield trends by using the five year Olympic average of proven yields.

As of June 16, 2010, we were advised by FSA staff that 136,170 farms will be participating in the ACRE program for the 2010, 2011, and 2012 crop years. In ACRE's initial year, the share of farms nationwide was around eight percent comprising almost thirteen percent of base acres, well below initial projections by the Congressional Budget Office. While NCGA expressed its concerns last year with the preparedness of Farm Service Agency county offices to adequately explain the ACRE program, our growers have indicated far fewer problems this year. Nevertheless, we believe a more concerted effort is necessary to provide FSA employees the training resources and office support systems to help streamline the enrollment process and program compliance. Some of the concerns regarding ACRE that we hope USDA and this committee will take under consideration include the farm eligibility condition and the procedures for growers to document their yields. In some cases, reorganization of farms and time itself will reduce producers' use of county yield plugs in the absence of a proven yield to establish a farm's benchmark revenue.

A recent Iowa State study asked farmers who did not participate in ACRE why they decided to decline this option. Complexity was listed as the major reason for not participating. Despite the fact ACRE is modeled, in part, after popular revenue insurance policies, it is not surprising that many producers find the rules requiring landowner approvals and documents to prove yields overly burdensome. Plus, the double trigger, requiring state revenue to be below a state guarantee and farm revenue to be below a farm guarantee adds to the program's complexity. While the farm eligibility condition helps to ensure payments are targeted for real losses, the removal of this requirement would substantially reduce the FSA's work load and administration costs. Moreover, the farm level trigger adds a moral hazard problem. In some cases, farmers could have an incentive to assure the farm trigger is met given expectations that the state trigger will be met.

Another important administrative related issue for ACRE is the limited and inconsistent data collected by the National Agriculture Statistics Service (NASS) used to compute a state's crop revenue values. This is not only a problem for ACRE, but for counties where producers no longer have access to area wide crop insurance plans due to insufficient production data. As an example, a corn grower in Arkansas who would have elected ACRE on dry land corn in 2009 will find out that for 2010 Arkansas corn ACRE will be a combined practice because Arkansas did not meet the 25 percent irrigated acre requirement for 2010. There is the possibility that the coverage could be restored in 2011, but a farmer in this case has elected ACRE assuming a dry land yield. Another example of insufficient NASS data can be found in Oklahoma where the state has published state level dry land and irrigated yields for about ten years. In ACRE's initial year, NASS only published a combined yield, but ACRE is split between irrigated and dry land for Oklahoma corn.

Over the next few months, NCGA will be evaluating a number of design changes to enhance ACRE. They include the use of futures prices for determining guarantees and revenues which could more effectively combine ACRE with marketing practices. Further, use of the season average price causes almost a year's delay in receiving ACRE payments. Another alternative is the harvest price now used in crop insurance. Absent any change to the price component in the guarantees, a five percent cup instead of a ten percent cup provides support for a longer period of time when revenue declines over continuous years. Our growers are also very interested in basing the ACRE on county yields rather than state yields as they more closely reflect farmers' yield risk. Notwithstanding the production data issues previously mentioned, we recognize this one change, alone, will likely require a significant trade-off, assuming no additional funding for the commodity title.

Other suggestions that have been offered to simplify ACRE include: 1) calculating the revenue target as a five year moving average rather than as a five year Olympic average and a two year moving average of price. 2) Eliminate the base acre cap to make all planted acres eligible for payments. 3) Use the same method to determine the farm and state benchmark revenues to eliminate the potential disconnect between the risk management assistance at the broader market area and individual farms. 4) Change to a national program to allow for other enhancements that would not be possible due to budget constraints.

The other major addition to the farm safety net was the disaster assistance program, Supplemental Revenue Assistance (SURE). In our view, it represents an improvement over ad hoc disaster programs. SURE introduces more certainty and takes a much needed step toward eliminating duplicate payments for the same revenue losses.

SURE represents an effort at a comprehensive revenue assurance program: it covers whole farm revenue for both covered commodities and many other crops; it includes crop insurance indemnities, Noninsured Crop Disaster Assistance Program (NAP) payments, Marketing Assistance Loan proceeds, Direct and Counter-cyclical Program (DCP) payments and ACRE payments. SURE revenue is guaranteed at 115 percent of purchased crop insurance coverage levels, raising revenue protection up to a maximum of 90 percent and it provides protection for both the growing season and the marketing year of a crop, relative to the growing season coverage of crop insurance and the marketing year coverage of ACRE.

Substantial assistance has been received by a number of farms, however, there is a concern of a moral hazard over a requirement of ten percent yield loss for one crop despite that all other SURE requirements are met. When the difference between a substantial payment and no payment is dependent upon a ten percent yield loss for one crop, an incentive exists for a producer to reach the ten percent yield loss.

The design of SURE also raises questions of equity for farmers who operate multi-crop operations. Aside from other serious issues of program complexity and long term funding, concerns remain about overlapping coverage with ACRE and crop insurance. According to one analysis by Drs. Carl Zulauf, Gary Schnitkey and Michael Langemeir, the overlap between these programs is not large due to their different parameters. Most of the overlap occurs between SURE and ACRE due to the same coverage level of 90 percent. One possible solution for addressing most of this overlap is to change SURE's payments to harvest time.

Other observers have noted that crop insurance, ACRE and SURE all have a similar purpose to provide an effective safety net to producers, but have many differing program components and requirements that could be harmonized so as to provide a combined set of programs that would improve overall coverage will minimal overlap. Different entity definitions and coverage units could be unified; a similar price reference across programs could be used; coverage levels are similar, but could be combined to include shallow losses. This would clearly be no small undertaking, but elective programs that were better harmonized could improve the risk management safety net and leave fewer gaps.

Moving forward, NCGA believes enhancements to ACRE and our crop insurance programs could effectively address the gaps SURE is designed to cover today. We understand that achieving a farm safety net that would significantly diminish the need for disaster assistance is an elusive goal yet is one worth pursuing. Given the fiscal challenges that lie ahead and the increasing importance of risk management tools, NCGA appreciates this Subcommittee's consideration of our members' concerns and looks forward to working with you and your staff as you prepare for the next farm bill.