

# Agricultural Economic and Policy Perspectives

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## The Effects of Payment Limitations on Acreage

Although the Farm Security and Rural Investment Act (FSRIA) of 2002 was signed into law more than a year ago, the debate over limits on farm program payments continues. In response to increased attention from the public, some members of Congress have proposed legislation tightening limits on farm program payments. One such bill, S. 667 — introduced by Sen. Charles Grassley (Iowa) — will, if passed, reduce the limit on fixed direct payments to half the current amount, reduce the counter-cyclical payment limit by more than half, and limit loan deficiency payments through tighter restraints on the use of generic commodity certificates. The substantially lower limits are not likely to have a large impact on corn, soybean, and wheat farmers; however, rice and cotton farmers in the South could feel a significant impact from S. 667.

The Federal Agriculture Improvement and Reform (FAIR) Act of 1996 implemented decoupled, fixed payments and eliminated deficiency payments, providing a safety net for farmers during a time of relatively high commodity prices. Under the FAIR Act, total program payments under the three-entity rule were limited to \$225,000, with plans to decrease support over the life of the bill (although generic commodity certificates were included). The decoupled, fixed payments were scheduled to expire with the bill, but after a drop in commodity prices after the bill became law, Congress doubled the limit on both decoupled, fixed payments and loan deficiency payments. By 2002, the limit on government payments was more than double the original limit of the FAIR act.

(See Payment Limitations on page 2)

## Impact of New Tax Cuts on Farming Families

On May 28, 2003, President Bush signed the Jobs and Growth Tax Relief Reconciliation Act of 2003 into law. This income tax bill accelerates tax rate reductions that were scheduled to be phased-in under a previous tax relief act signed in 2001. The act both reduces the tax rate on dividends and capital gains and increases the amount that can be expensed by small businesses on capital investment.

This act, although not specifically designed for agriculture, is expected to result in a roughly \$4 billion reduction in federal income taxes paid by farm households this year. The reduction in taxes for farm households in 2004 is expected to be somewhat larger. Over 86 percent of farming households will receive some form of tax reduction through this bill. USDA estimates the average income tax savings per farming household to be about \$2,000. In a recent USDA report, five areas of the bill are identified as contributing to the tax reduction for American agriculture: (1) acceleration of the 2001 tax relief act, (2) re-

duced tax rate on dividends, (3) reduced tax rate on capital gains, (4) increased expensing of capital investment, and (5) alternative minimum tax relief.

The 2001 tax relief bill was originally scheduled to be phased-in over a span of four years, beginning in 2005. The Jobs and Growth Tax Relief Reconciliation Act of 2003 accelerates the tax cuts in the 2001 bill to begin immediately. The original bill included provisions such as an expansion of the 10 percent tax bracket for joint returns; a reduction in current marginal tax rates; an increase in the standard deduction and width of the 15 percent bracket for married couples; and an increase in the child tax credit from \$600 to \$1,000. The accelerated cuts are estimated to reduce the tax burden placed on farming households by \$2.3 billion in 2003.

Tax rates will be reduced on both dividends  
(See Tax Cuts on page 3)

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## Payment Limitations

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The current farm bill, written during a time of increased public concern about government support of agriculture, decreases the payment limits from the amended FAIR Act's \$460,000 to \$360,000. Although the total payment limits

**Table 1. Total Farm Program Payment Limits: 1996—2002**

Payment Type	FAIR 1996	FAIR 2000	FSRIA 2002
PFC/Direct	\$40,000	\$80,000	\$40,000
Counter-Cyclical	n/a	n/a	\$65,000
Loan Deficiency	\$75,000	\$150,000	\$75,000
Total Limit*	\$115,000	\$230,000	\$180,000
Commodity Certificates	Yes	Yes	Yes

\* Total limit for a single entity. Under the three-entity rule, a producer is able to double these limits.

were decreased in the 2002 farm bill, FSRIA included provisions continuing the authorization of generic commodity certificates, effectively removing the limit on loan deficiency payments. Table 1 shows the differences in payment limitations found in the FAIR Act and FSRIA. The FAIR Act of 1996 and FSRIA include similar payment limits, but the addition of counter-cyclical payments in FSRIA increases the limits by \$65,000 for a single entity. Total payment limits of FSRIA are \$50,000 lower than those of 2000. However, since producers can use generic commodity certificates, there is effectively no limit on loan deficiency payments. Thus, producers can actually receive \$25,000 more in program payments under FSRIA than they could under FAIR in 2000 (\$105,000 in direct and maximum counter-cyclical payments under FSRIA compared to \$80,000 in PFC payments under FAIR).

The most pronounced opposition to existing payment limitations has surfaced in the Midwest, primarily from Senators Grassley and Dorgan (North Dakota). After their primary attempt to limit farm program payments failed (Grassley-Dorgan amendment to the Senate farm bill), Senator Grassley continued the push by introducing a new bill similar to the original amendment co-sponsored by Senators Hagel (Nebraska), Johnson (South Dakota), Dorgan and Daschle (South Dakota). This bill to tighten payment limits was introduced in March 2003, and would impose substantially lower limits than FSRIA. In this bill, identified as S. 667, the Senators propose limiting total payments to \$137,500 per entity by reducing fixed direct payments and counter-cyclical payments and by limiting generic commodity certificates. The three-entity rule would not be changed, allowing producers to effectively double the single-entity limit to \$275,000. Table 2 shows the proposed payment limits under S. 667. The direct payment limit is decreased from \$40,000 to \$20,000, and the counter-cyclical payment limit

is reduced from \$65,000 to \$30,000. Loan deficiency payment limits are increased from \$75,000 to \$87,500, but commodity certificates are only allowed up to that limit.

Farmers who produce commodities that receive relatively high levels of government payments per acre, such as rice or cotton, would be most affected by S. 667. Under current legislation, a cotton farmer with a 717-pound counter-cyclical yield and a 660-pound direct yield<sup>1</sup> would receive a counter-cyclical payment of \$83.68 per acre and a direct payment of \$37.42 per acre, resulting in total payments per cotton base acre of \$121.10 (not counting any loan deficiency payment). In contrast, a soybean farmer with a 29 bushel counter-cyclical yield and a 24 bushel direct yield would receive a counter-cyclical payment of \$7.65 per acre and a direct payment of \$9.35 per acre, for a total payment per soybean base acre of just \$17.00.

The higher per acre payment for cotton means that a cotton farmer is subject to reach payment limitations at a lower total acreage than farmers of most other commodities. Acreage restrictions also occur in soybean farming, but even with the restrictions proposed in S. 667, soybean farms can reach sizes more than nine times the size of cotton farms without exhausting the limits for counter-cyclical payments. Farmers with a 29-bushel soybean program yield will reach payment limitations for counter-cyclical payments at 5,747 acres. Cotton farmers, however, would reach counter-cyclical payment limits at 609 acres with a 717-pound program yield. Figure 1 shows the differences in the minimum acreage required to reach pay-

**Table 2. Government Program Payment Limits Proposed in S. 667**

Direct Payment	\$20,000
Counter-cyclical Payment	\$30,000
Loan Deficiency Payment	\$87,500
Total Limit*	\$137,500
Commodity Certificates	Limited

\* Total limit for a single entity. Under the three-entity rule, a producer is able to double these limits.

ment limitations under both FSRIA and S. 667. Direct payments are calculated using a 660-pound program yield for cotton and a 24-bushel program yield for soybeans.

(See Payment Limitations on page 3)

<sup>1</sup> Provisions in FSRIA allowed producers to update the program yields used to calculate counter-cyclical payments but not the yields used to calculate direct payments. For this reason, it is possible for the same farm to have two different program yields—one for the counter-cyclical and another for the direct payment—as in this example.

## Payment Limitations

(Continued from page 2),

FSRIA also mandated the creation of a commission to study the impact of changes to payment limitations on the farm sector. The Commission on the Application of Payment Limits for Agriculture held a public workshop on June 17, 2003, where presentations on analyses of payment limit proposals were made by several academic specialists as well as representatives from the National Cotton Council and the Food and Agricultural Policy Research Institute (FAPRI). Analysis of the same provisions as those in S. 667 presented by FAPRI found that 44 percent of the rice farms and 23 percent of the cotton farms in its model would have at least one type of payment limited, assuming these farms made no adjustment as a result of changes in payment limitations.

Furthermore, FAPRI analysis found that only 1 to 3 percent of the sorghum, wheat, corn, and soybeans farms in its model would be similarly affected by changes to the payment limitations.

Clearly, rice and cotton are affected much differently by changes to payment limits than are most other program crops. Consequently, much of Mississippi's farm sector is very interested in this issue. The Department of Agricultural Economics at Mississippi State continues to analyze the impacts of changes to payment limits on Mississippi farms.

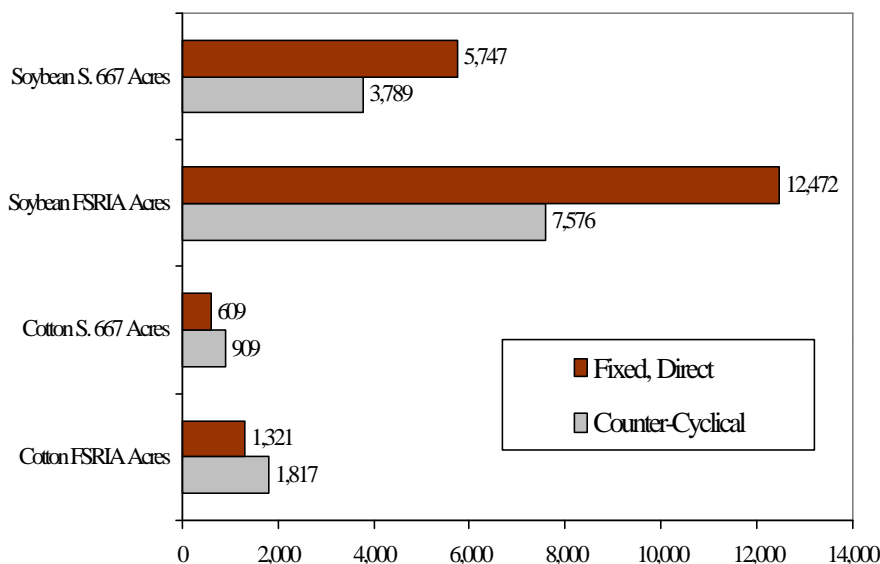
## Tax Cuts

(Continued from page 1)

and capital gains. Dividends paid to individuals will be taxed at 15 percent. For taxpayers in the 15 percent or lower income tax brackets, the tax rate on dividends will be reduced to five percent. The reduction in the tax rate on dividends will affect about one third of all farm households and more than half of those households with a farmer over 65 years of age. Savings on taxable dividends are estimated to reach \$700 million in 2003. Capital gains taxes are also reduced to 15 percent and as low as five percent for taxpayers in the 15 percent or lower tax brackets. Internal Revenue Service data suggests that 45 percent of all farmers report some capital gains. Since the capital gains tax cuts only apply to sales on or after May 6, 2003, estimated savings for this year are \$500 million with an expected increase to over \$750 million in 2004.

The bonus first-year depreciation is raised from 30 to 50 percent and increases the amount of investment that can be ex-

**Figure 1. Minimum Acreages to Reach Payment Limits: Soybeans and Cotton**



Additionally, the Commission on the Application of Payment Limits for Agriculture plans to issue its final report in the near future. Senate bill 667 was referred to the Committee on Agriculture, Forestry, and Nutrition on March 19, 2003 and awaits further action. Further information on the bill and its current status can be found by visiting <http://thomas.loc.gov>.

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pensed from \$25,000 to \$100,000. In 2003, the depreciation increase will allow more than 90 percent of purchases of farm machinery made after May 5, 2003, to be immediately deducted. An estimated 98 percent of all farmers will be able to deduct their entire investment. Savings for 2003 are expected to reach \$3.5 billion, and federal income and self-employment taxes paid by farmers should decrease by nearly \$1 billion. Farm families may also benefit from the alternative maximum tax exemption, which increases by \$9,000 for married taxpayers and by \$4,500 for single taxpayers in 2003 and 2004.

USDA recently issued a press release summarizing their analysis of the 2003 tax cut package. The full press release as well as further information on the tax cuts are available on the USDA's website ([www.usda.gov](http://www.usda.gov)). Additional information can also be found in the *Doane's Agricultural Report* for June 6, 2003.

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## Upcoming Events

**Farm Bureau Summer Commodity Conf.**  
July 7-8  
Jackson, MS

**Teacher's Conference**  
July 9-11  
Starkville, MS

**MS Boll Weevil Annual Meeting**  
July 12  
Grenada, MS

**Master Gardener Training in Central MS**  
July 15-16  
July 21-25  
Raymond, MS

**State 4-H Cooperative Business Tour**  
July 22

**State 4-H Teen Leadership Conference**  
July 28

## USDA Reports Calendar

**July 3**

Dairy Products

**July 7**

Poultry Slaughter

**July 10**

Vegetables

**July 11**

Crop Production

**July 17**

Farm Production Expenditures

Milk Production

**July 18**

Livestock Slaughter

Cattle on Feed

Cold Storage

**July 22**

Catfish Processing

Chicken and Eggs

**July 25**

Monthly Agnews

**July 28**

Farm Computer Usage and Ownership

**July 31**

Agricultural Prices

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