Considering the impacts of eliminating the Harvest Price Option

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Summary of Findings:

- Rep. John Duncan (R-TN) of the House of Representatives, and Jeff Flake (R-AZ) and Jeanne Shaheen (D-NH) in the Senate of the United States have introduced legislation to eliminate the Harvest Price Subsidy included in Section 508(e) of the Federal Crop Insurance Act (7 U.S.C. 1508(e)).
- The bill introduced to prohibit the Harvest Price Subsidy is known in the House as H.R. 4305-Harvest Price Subsidy Prohibition Act. In the Senate, it uses the same name but it is classified as S. 2096.
- The Federal Crop Insurance Act (7 U.S.C. 1508(e)) states the purpose of subsidizing a portion of crop insurance through legislations is to encourage maximum participation of producers in catastrophic risk protection.
- Insurance payments to producers are made when the harvest price exceeds the planting price of the crop and there is a yield decrease.
- Opponents of the legislation argue that the HPO provides a safety net for agricultural producers, especially those who forward contract (i.e. sign contracts for the sale of their crop before real harvest prices are known), in case of crop failure.
- Proponents of the legislation argue the current Harvest Price Option (HPO) overburdens taxpayers, who stand to save $21.1 billion over ten years, according to figures from the Congressional Budget Office, if the legislation is passed.

Background

The Harvest Price Option (HPO) is a popular choice among crop producers in the United States. Most producers purchase Revenue Protection (RP) insurance (Schnitkey et al, 2017). The HPO is a payment made to producers who have purchased this type of insurance when revenue at harvest is less than the revenue of the coverage (i.e., when the harvest price is less than the spring planting price). Agricultural economists at the University of Illinois conducted an historical analysis of projected and harvest insurance prices between 1974 and 2016 and found the insurance price of corn exceeded the harvest price 37% of the time (Schnitkey et al, 2017). In those years when HPO was paid out (when harvest price was less than the spring planting price), the harvest prices were 16% higher than the projected price.

It is important to note that harvest price at below the projected price alone will not set off insurance payments. There must also be a decrease in the yield registered for that year (Schnitkey et al, 2017). The rationale behind this logic is that yield decreases will lead to a drop in the supply, which will increase the price for the crop. Producers who signed contracts at the beginning of the crop season are guaranteed the harvest price for their product, and those who forward contract or feed their crop to livestock are protected against having to pay high prices to purchase corn promised in a contract or to feed their animals after a crop failure. Thus, HPO is one of a suite of risk management tools available to farmers to mitigate risk. However, in times of high crop prices, this tool has also resulted in farmers assuming unnecessary risk, such as farming on marginal lands (e.g. wetlands and drylands).
because they were guaranteed to claim insurance at a high price even if they suffered large losses (Redlin, 2018, personal communication).

**What are the key changes to current farm subsidy payouts?**

The bills presented in the legislature propose to eliminate taxpayer contributions to the subsidy that producers receive through the crop insurance program in the form of the HPO. Justification for taxpayer participation in this program is based on the argument that taxpayers benefit by ensuring a secure food supply. Opponents of taxpayer participation argue that alternative safety net programs exist even without the HPO (Clayton, 2017). However, supporters of HPO claim that it is an important financial risk management tool available to producers.

**Who will be affected by the changes and how?**

Taxpayers and producers are the main stakeholders involved in this legislative move. Taxpayers may save $21.1 billion dollars over ten years (Clayton, 2017). These funds could be appropriated to other priorities. Taxpayer advocates claim that removing this subsidy will protect taxpayers from abuses of the HPO (Babcock, 2016). The Congressional Budget Office (CBO) reported in December 2017 that taxpayers have gained relatively little from the program. A slight increase in the number of acres planted under the program could decrease the cost of food a little. However, a decrease in the price of commodities does not necessarily translate into lower food costs (CBO, 2017). Additionally, eliminating the HPO may help to preserve natural resources by removing incentives to practice agriculture on lands that promise only marginal production yield (Redlin, 2018, personal communication). Natural resources, a public good, would be better protected against exploitation.

On the other hand, crop producers will lose a financial risk management tool and must rely on other mechanisms to protect themselves from unfortunate financial situations. The Farm Bureau highlights the situation of crop producers who sign contracts at spring planting (forward contracting) who are responsible for delivering the crop to the buyer, even if they experience a failed crop that year. In this case, the producer must purchase grain, likely at an elevated price due to limited supply, and deliver it to the buyer. This kind of mechanism may prevent passing down costs to the consumer, ensuring that prices at the store remain stable. The CBO found that for the 2002 and 2016 period, farmers received $65 billion more in payouts than they paid in premiums to the crop insurance program. This highlights how farmers are benefiting from the existing program.

**Summary**

The 2018 Farm Bill faces scrutiny as comes up for renewal. The Harvest Price Option (HPO), which uses taxpayer and producer dollars through the Federal Crop Insurance Program, is being considered for elimination. Removing the HPO from the risk management tools offered by the U.S. government to U.S. farmers could result in significant savings for the national budget. Consequences of this change to the Federal Crop Insurance program may be felt by U.S. producer communities and consumers. Current government risk protection for farmers limits catastrophic losses and maintains a steady supply of food and fiber. This encourages the prosperity of America’s farming communities and food security for its citizens. At the same time, the government is called to exercise fiscal responsibility, which may include reforming existing programs such as the HPO. Evaluation of alternative options, such as those provided by the CBO in their 2017 report to Congress, provide potential paths forward towards meeting competing objectives to reduce spending and mitigate risk.
References