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The Importance of Farm Program Payments to Farm Households

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- Less than half of all farms—43 percent—in 2005 received farm program payments.
- Large family farms represent 8 percent of all farms, but they received 58 percent of commodity program payments going to farms.
- Two-thirds of recipient farms received less than \$10,000 in payments, accounting for only 7 percent of their gross cash farm income. Payments represent 13 percent of gross cash farm income for those that receive more than \$30,000 in payments.

From 2000 to 2005, the farm sector received \$112 billion in government payments (measured in 2005 dollars) through an array of farm programs, including direct payments, countercyclical payments, loan deficiency payments, emergency payments, and conservation payments. These payments provide income support for eligible farm operators and farmland owners, with eligibility and payment criteria varying by program (see box, "Some Farm Program Payments Vary More Than Others").



Lynn Betts, NRCS/USDA

While farm program payments go to a variety of farm operators and owners for many reasons, less than half of farm operators receive any payments. And, of those that do, in most cases, these payments are relatively modest. About 15 percent of farm households received \$10,000 or more in farm program payments in 2005. Given the uneven distribution of farm program payments and their variability over time, what do we know about farm program payment recipients and the importance of these payments to their business operations and household well-being?

While program payments can have sector-wide effects on land values and commodity prices, and can directly affect many nonfarm-operator households, such as nonoperator landlords, our primary focus is on the characteristics of farms and farm operator households receiving the payments. In 2005, the average payment among farms receiving program payments was \$18,000, with large farm operations (those with sales of \$250,000 or more) receiving an average of nearly \$70,000. Nonetheless, this may overstate the importance of program payments to large farms and their operators for several reasons.

Farms receiving program payments often lease a sizeable portion of the land they operate and are more likely to have more than one household involved in operating the farm. Payments tied to the land are likely to accrue, directly or indirectly, to the landowners given enough time for rental rates to adjust. And even when the operators own all the land they farm, having multiple households involved in the operation dilutes the importance of program payments to each individual operator. Furthermore, program payments do not reflect the added costs farm operations incur to receive payments from many farm programs. Finally, the importance of program payments to the farm household's well-being declines as nonfarm income grows. Most operators and other household members of farms receiving program payments have significant off-farm sources of income, making income from farming and program payments less important.

Large Farms Receive Most Commodity-Related Payments

Most of the value of U.S. agricultural production comes from large family farms. By contrast, most U.S. farms are small family operations with less than \$250,000 in sales. Federal farm programs do not

explicitly target payments to farms of a certain size or net income level, although caps may apply to the size of the program payment a farm or an individual farmer can receive. Nevertheless, large farms are more likely to receive farm program payments and, as a group, they receive the bulk of payments simply because most payments are paid per acre. Current payment limits affect a very small percentage of farms (see box, "Data Source and Farm Types").

Three-quarters of large family farms receive farm program payments, compared with just over half of small commercial farms and a third of residential/retirement farms. Large farms' high participation rate reflects their heavy enrollment in commodity-related programs that are targeted at current or past production of commodities. In contrast, smaller farms are most likely to specialize in cattle, particularly cow/calf operations, and in other commodities which are generally ineligible for commodity-related payments. Despite a higher percentage of large family farms receiving farm program payments, however, most of the farms receiving farm program payments are small, reflecting the 91-percent share of farms in the two small-farm groups.

Anson Eaglin, USDA

Some Farm Program Payments Vary More Than Others

Payments are made through numerous government farm programs, each with its own goals and eligibility criteria. Payment programs also vary in the method used to determine the dollar value of disbursements. The actual distribution of payments to farms in any year is the result of the combination of the eligibility criteria, payment calculation methods of the programs working in tandem with market and weather conditions, and production and management choices of individual operators.

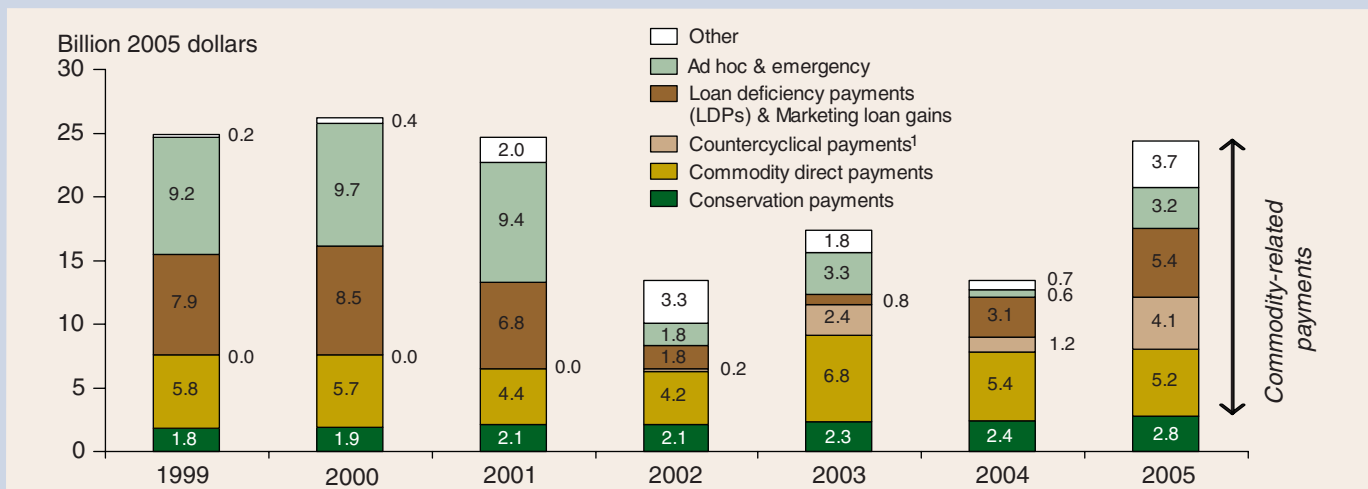
Commodity direct payments have ranged between \$4 billion and \$7 billion since 1999. These payments are based on a producer's historic acreage and yield of a particular commodity, not on current production or prices. To be eligible for direct payments, a farm must have an official historical record of base acreage and program yield for wheat, feed grains, rice, cotton, or oilseeds. Direct payments—and the production flexibility contract payments (PFCs) that preceded them—are relatively stable over time because they are not based on current production or prices.

Countercyclical payments, which accounted for another large share of all payments in 2005, are paid on the same base acreage and program yields as direct payments, but are linked to current market prices. In contrast, loan deficiency payments (LDPs) and marketing loans are fully linked to both current production and market prices because they are paid on total production of the commodity. Because these programs are linked to market conditions, their annual disbursements are highly variable. In 2005, LDPs and marketing loans accounted for 39 percent of total payments.

Emergency payments are the most variable among the farm programs. For example, crop failures due to weather conditions helped push emergency payments to \$9.7 billion (37 percent of total payments) in 2000. In contrast, emergency payments amounted to \$0.6 billion (5 percent of total payments) in 2004. In some years, emergency payments can significantly increase the number of farms receiving payments, especially if the distressed farms produce commodities like beef cattle and specialty crops not otherwise covered by a program.

Payments from the largest conservation program, the Conservation Reserve Program (CRP), are relatively stable. The most common type of CRP payment arrangement is a 10-year fixed annual rental rate. The CRP pays landowners rent for taking land out of production and engaging in conserving uses. The CRP is voluntary, but receipt of CRP payments is based on a competition to supply the greatest environmental value to the public from the land put in conserving uses.

Compared with other types of farm program payments, conservation payments and direct payments are relatively stable



Note: This figure includes payments made to all recipients, both those who farm and those who do not.

¹ Includes the similar Production Flexibility Contract Payments (PFCs) that preceded direct payments.

Source: USDA, Economic Research Service, U.S. and State Farm Income Data.

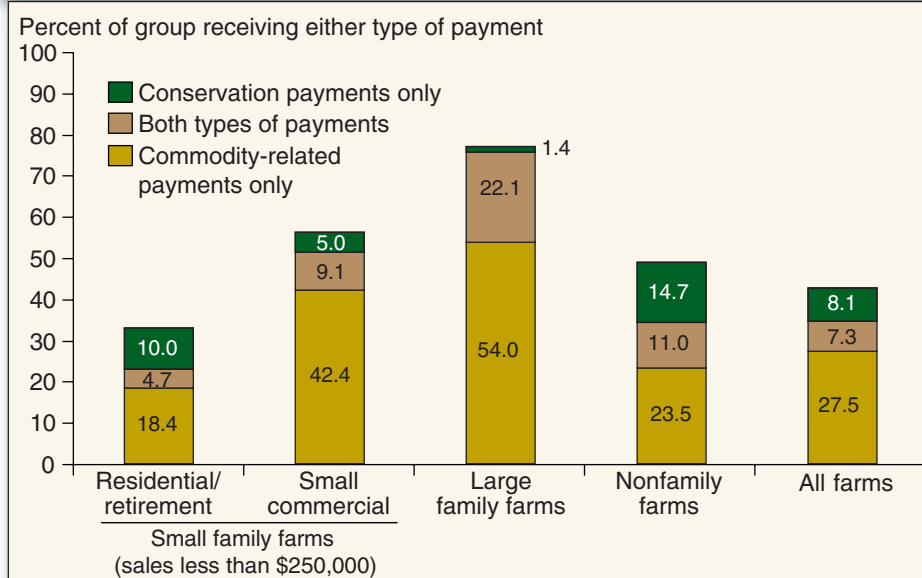
Data Source and Farm Types

Data from the Agricultural Resource Management Survey (ARMS) offer significant advantages when addressing questions of how farm program payments are distributed among farms because the survey can identify both participating and nonparticipating farms. Unlike other data sources, ARMS also provides detailed information on the farms' financial and production characteristics in conjunction with the characteristics of farm operators and their households. Since ARMS contacts only farm operators, however, analysis based on ARMS data examines the distribution of farm program payments that actually go to farms during a calendar year. It excludes the payments made to people who do not farm, mainly nonoperator landlords.

Most of the data reported here are from the 2005 ARMS. Data are reported by farm type, which reflects the organization and sales class of the farm and the principal occupation of the farm operator, as follows:

- **Family farms.** Farms organized as sole proprietorships, partnerships, or corporations where at least 50 percent of the stock is held by related persons and which do not have hired managers (98 percent of farms; 85.4 percent of production).
- **Small family farms.** Sales less than \$250,000 (90.5 percent of farms; 22.8 percent of production).
 - **Residential/retirement.** Operator reports spending the majority of work time at a nonfarm occupation or is retired (64 percent of farms; 7 percent of production).
 - **Small commercial.** Operator reports spending the majority of work time at farming (26.5 percent of farms; 15.8 percent of production).
- **Large family farms.** Sales of \$250,000 or more (7.5 percent of farms; 62.7 percent of production).
- **Nonfamily farms.** Farms organized as nonfamily corporations or cooperatives, as well as farms operated by hired managers. Also includes farms held in estates or trusts (2 percent of farms; 14.6 percent of production).

A greater share of large family farms received farm program payments as compared with other farms in 2005



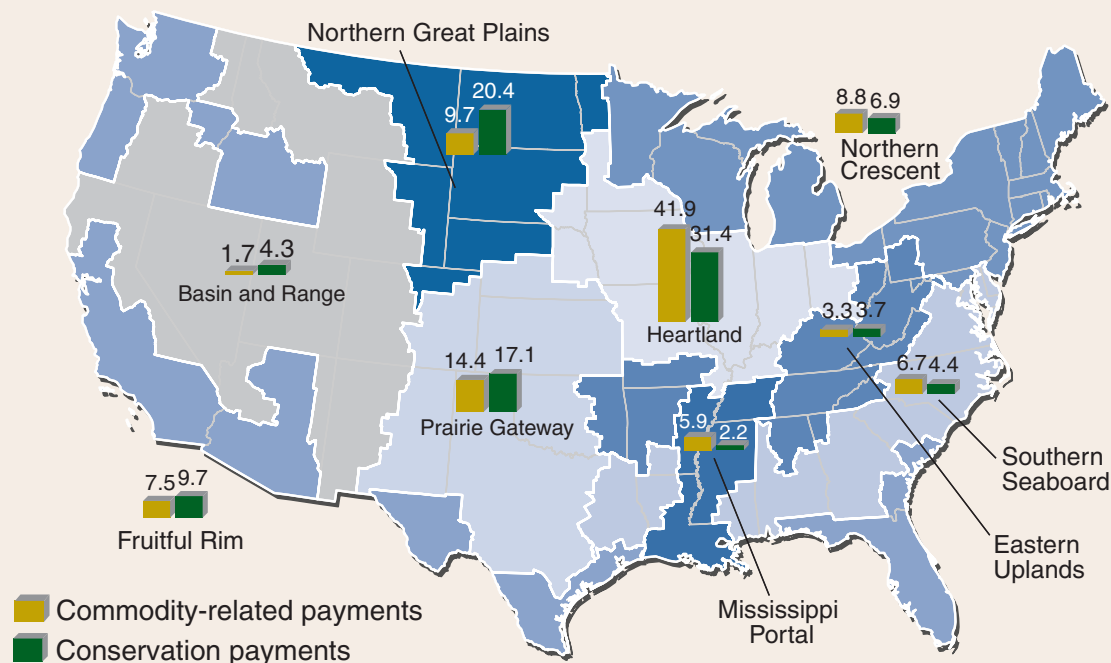
Source: USDA, ERS, 2005 Agricultural Resource Management Survey, Phase III.

The distribution of commodity-related payments corresponds to the production of program commodities (in terms of market value). For example, 58 percent of commodity-related payments go to large family farms which, as a group, produce 61 percent of program crops. Commodity-related payments are also heavily concentrated geographically. Farms in the Heartland receive about 42 percent of commodity payments, which is in line with the region's 50-percent share of production of program crops.

Residential/retirement farms comprise nearly two-thirds of all farms and receive about half of all conservation payments. Given that the CRP accounts for 82 percent of conservation payments and is paid on a per acre basis, it may be surprising at first

Farms in the Heartland received the largest share of both commodity-related and conservation payments in 2005

Percent of total payments to farms, by payment type



Source: USDA, ERS, 2005 Agricultural Resource Management Survey, Phase III.

glance that residential/retirement farms—with their small average acreage—account for half of all conservation payments. Even though they have small acreages, participating residential/retirement farms enroll larger shares of their land in CRP than other program participants. For example, CRP enrollments account for 47 percent of the land operated on participating residential/retirement farms, compared with only 6 percent on participating large family farms. Large-farm operators likely enroll such a small share of their land in the CRP because the opportunity cost of removing their land from production is high, except on the most environmentally sensitive land.

Limited Contribution to the Bottom Line

Farm income is more variable than the wage and salary income relied upon by the typical U.S. household. One of the functions of farm program payments is to provide a cushion to income variability over time; indeed, some payments are designed mainly for that purpose. How important are farm program payments to the overall financial position and income stability of farm operator households? The short answer—it depends, but for most farm operator households, farm program payments account for a relatively small share of cash receipts and play only a minor role in smoothing out the effect of

variable farm incomes on farm household well-being.

The majority of farm operator households operate farms that do not receive farm program payments, and for most of those that do receive program payments, those payments total less than \$10,000. To put this into perspective, the average off-farm income of the 85 percent of farm households receiving no program payments or less than \$10,000 in payments is roughly \$70,000 and the average household net worth is over \$700,000. Therefore, off-farm income and accumulated household wealth play a much larger role in maintaining farm household income and reducing the effects of year-to-year variability in farm income than farm program payments for most farm households.

Only 15 percent of farm households operated farms that received more than \$10,000 in farm program payments in 2005

Item	Payment level for farm operated—				All farm households
	No payments	Low (less than \$10,000)	Medium (\$10,000 to \$29,999)	High (\$30,000 or more)	
	<i>Number</i>				
Number of operator households	1,174,578	576,931	163,025	138,662	2,053,196
	<i>Dollars per household</i>				
Average farm household income	76,371	72,306	83,464	159,699	81,420
From farming	3,584	6,921	33,066	118,705	14,637
From off-farm sources	72,787	65,385	50,398	40,994	66,782
Average household net worth	731,221	762,048	1,081,531	1,785,149	838,875
	<i>Dollars per farm receiving payments</i>				
Average farm program payment	0	3,116	17,771	76,866	na
	<i>Percent of operator households that...</i>				
Share income with another household	1.3	2.8	7.3	10.4	2.8
na = Not applicable.					
Note: Excludes nonfamily farms. Household income and net worth are not estimated for nonfamily farms.					
Source: USDA, ERS, 2005 Agricultural Resource Management Survey, Phase III.					

Of course, not all farms are close to "average." Fifteen percent of farms received \$10,000 or more in farm program payments in 2005. This group included a mix of all types of farms, but payments tended to increase in tandem with farm sales—most of the farms receiving \$30,000 or more in payments were large family farms. For this last group of high-payment farms, the average payment was \$76,900. This is four times the average payment of all farms receiving payments in 2005. When the cost of participating in farm programs is considered, however, the importance of farm payments to the well-being of even these high-payment farm households is likely to be overstated.

Unlike unemployment insurance or Social Security, farm program payments do

not always translate dollar-for-dollar into household income for three reasons. First, receipt of some farm program payments may require that producers incur additional farm expenses or forego commodity income. This is the case with the CRP, for example, where producers must set aside land for conservation to be eligible for payments. The payment is not "on top" of receipts from the sale of commodities but replaces commodity sales. In effect, CRP participants provide environmental benefits for society instead of crops for the marketplace. Other conservation program payments reimburse the farmer for part of the cost of adopting conservation farming techniques, so receipt of payments may actually reflect a net loss to the farm busi-

ness. The receipt of some commodity program payments is only possible if the farmer grows a crop, so higher payments require higher input costs. The only payments that add dollar-for-dollar to the bottom line of the business are direct payments which, in 2005, amounted to roughly 21 percent of total payments.

Second, large farms are more likely to lease the land they operate. Fifty percent of farms receiving program payments rented at least part of the land they operated, with larger farms leasing more often and leasing a higher percentage of their operations. In comparison, 30 percent of farms not receiving program payments lease land. While the extent to which farm programs are capitalized into land values and

lead to higher rental rates is uncertain, it is likely that some of the payments pass through to nonoperator landlords. Thus, even for direct payments, the farm operator household likely benefits less than dollar-for-dollar.

Third, net income from large farms is more likely to be shared among multiple households than net income from smaller farms. This means that if households operating large farms participate in government farm programs, they are more likely to share the government payments, too, reducing the proportion of each household's income attributed to government payments. Fourteen percent of households operating large farms that receive government payments reported sharing income with other households, compared with only 3 percent for all farm households. The presence of multiple households begs the questions of how financial management decisions are made and what role government payments play in that context. These questions are yet to be fully understood but do seem to suggest a diminishing role for government payments within this larger financial context.

These measurement issues are difficult to adjust for, but by focusing on the size of farm program payments relative to gross cash farm income, researchers can

get a better picture of the relative importance of payments to recipient households. Most farm households received less than \$10,000 in payments, with the average for this group being slightly over \$3,000. Payments for this group averaged 7 percent of gross cash farm income. At the other extreme, for farms receiving more than \$30,000 in program payments, these payments represented 13 percent of gross cash farm income on average.

Averages can be deceiving, since there are farms for which program payments represent a larger share of receipts, and their numbers change from year to year. But considering that government payments to the farm sector were at a high level (\$24.3 billion in 2005), and that the sector's gross value of production was fairly typical of recent years, the well-being of relatively few farm operator households appears to be dependent on program payments.

Most farms—57 percent—do not receive farm program payments, although payments affect all farms indirectly by their influence on markets (e.g., commodity prices, land values and rents). On the other hand, since about 95 percent of the income for nonparticipating farm households comes from off-farm sources, these households are directly affected by general economic and tax policies. In fact, given the

importance of off-farm income to most farm households, economic policies affecting the local economy are important regardless of participation in farm programs. **W**

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