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BRIEF EXPLANATION AND WORKSHEET TO EVALUATE CORN PRODUCERS
PARTICIPATION DECISION
IN THE 1986 USDA FEED GRAIN PROGRAM ¹

By
Jim Hilker, Gerry Schwab, and Roy Black²

I. Introduction and Purpose of the Paper

Corn producers have several production/marketing alternatives for the 1986 crop year. The 1986 Feed Grains Program provides two distinct production/marketing alternatives for corn producers. One alternative is to participate by retiring the required 20% corn base acreage and growing corn on the remaining 80% of base acreage. The second alternative is to produce corn on at least 40% of the base acreage, but grow a non-program crop on the acreage remaining after corn and the required retired acreage are allocated. The third obvious alternative is to not participate in the Feed Grains Program. It is the purpose of this paper to briefly explain the program and evaluate participating in the program versus non-participation.

The program is administered by the local Agricultural Stabilization and Conservation Service (ASCS) Office. The sign-up period is March 3 through April 11, 1986.

II. General Purposes of the Feed Grain Program

- To reduce production and surplus stocks.
- To encourage exportation of U.S. feed grains.
- To provide support for net farm income.
- To provide a 'floor' below which corn prices are unlikely to fall.

III. Structure of Program for Corn

A. Eligibility

- To be eligible for the program benefits including the **deficiency payments, diversion payments and loans**, you must limit your 1986 corn acreage to no more than 80 percent of the farm corn base.
- The remaining 20% must be put under conservation practices; 17.5% is labeled unpaid acreage reduction program (ARP) and the remaining 2.5% is a paid land diversion.

¹ Paper includes program provisions known as of February 17, 1986.

² All authors are faculty members in the Agricultural Economics Department, Michigan State University.

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- You remain eligible for the program benefits as long as you plant at least 50% of your "eligible" acreage. "Eligible" acres are your base acres minus the unpaid ARP and the paid diverted acres. Another way of saying the same thing is that 40% of your corn base must be planted to corn (i.e., $40\% = (50\% * 80\%)$). Up to the other 41.4% can be planted to a non-program crop. Additional details on this provision are presented in Sections III.D.3 and V.C of this paper.

B. Restrictions

- Offsetting and cross-compliance will not apply to the 1986 Program crops.
- Contracts signed by farmers are considered legally binding for required participation.
- Haying will not be permitted on the retired acreage. However, the acreage may be grazed, except during the five principal growing months as designated by county USDA officials.
- Corn must first go into regular loan for nine months before it will be eligible for reserve loan and the storage payments of 26.5¢ per bushel per year made by the Commodity Credit Corporation (CCC). There can be a cap put on the Farmer Owned Reserve.
- A \$50,000 payment limitation per farm. However, the portion of the deficiency payment due to the price being below \$2.40/bu is not subject to this limit.

C. BASE Acreage and Yield Determination

- Your 1986 farm corn base will be the average of 1981-1985 acreage planted and considered planted to corn. **Considered planted** land is land that was diverted to conservation uses due to participation in the Feed Grains Program for corn.
- The program base yield will be an Olympic average of the last 5 years' program yields (not proven yields) i.e., dropping the high and low and dividing by 3.
- If you have not certified your base acres or yield 1 or more of the past 5 years, there will be an opportunity to do so. It will not be easy and perhaps frustrating. However, the payoff could be very high.

D. Income RISK Protection

- **Target price** is \$3.03 per bushel.
- **Loan rate** is \$1.92 per bushel.
- **Deficiency Payment Considerations**
 - 1) The **deficiency payment** per bushel equals the target price (\$3.03) minus the average farm price or the loan rate (\$1.92), whichever is greater. The maximum deficiency payment is \$1.11.

- 2) The **deficiency payment** is based on the national average farm corn price for the first five months of the corn marketing year if above \$2.40/bu or on the entire crop marketing year if less than \$2.40/bu.
- 3) If you plant less than the full 80% eligible to corn, you are still eligible for 92% of the deficiency payment provided 18.6% of your corn base acreage is retired and at least 40% of corn base is planted to corn. The 18.6% retired acreage is derived from the 2.5% paid land diversion plus 92% of the 17.5% ARP; i.e. $(18.6\% = 2.5\% + .92(17.5\%))$
- 4) You may request 40% of the USDA projected 1986 deficiency payments (\$1.03) when you sign up for the program. The deficiency payment cash advance will be reduced as 25% of the advance deficiency payment (or 10% of the total deficiency payment) is to be PIK. The cash deficiency payment may also be reduced because of the impact of the Gramm-Rudman bill. With an expected impact of the Gramm-Rudman at 4.3% reduction combined with the 10% PIK deficiency, the cash deficiency payment per bushel of base is approximately \$.887. $88.7\text{¢/bu} = \$1.03/\text{bu} \times (1-.043) \times (1-.10)$. The 40% cash advance is approximately 35.5 ¢/bu.
- 5) The 25% PIK deficiency payment will be received as generic in-kind certificate with specific monetary amounts. Producers with commodities under loan must use these commodities as PIK payment.
- 6) The generic in-kind certificates may be sold to other producers to replace loan, commercial firms or producers who are Co-op members.

- **Diversion Payment Considerations**

- 1) The payment rate for the 2.5% paid land diversion was set at 73¢/bushel. Total land diversion payment is 2.5% of (base yield x corn acres planted) times 73¢/bushel. The land diversion payment will be made in generic in-kind certificates, i.e., the value of the payment divided by the value of corn gives you the number of bushels.
- 2) The generic in-kind certificates will be available by county after May 1. Producers will have until September 30 or the maturity date of their loan whichever is earlier to redeem this certificate. CCC will value corn each day.

IV. Farm Variables Critical to Participation Decision

- A. Data that are unique to your farm and are critical to your decision on participation in the 1986 Feed Grains Program are:
 - Farm Program Base Historical Yield as compared to expected 1986 yield on total acreage and on reduced acreage.
 - Farm Program Base Acreage as compared to desired acreage for production purposes.
 - Expected market price for corn as compared to calculated break-even price given your farm's expected yield and associated variable cost of production and storage.

V. General Impressions of Three Alternatives

A. No Participation in Program

- Highest risk as all price and yield risk are carried by farmer.
- May be attractive to those who:
 1. Have low program base acreage relative to actual land available for corn production.
 2. Have low base yield relative to expectations of 1986 yields--not participating becomes relatively more attractive as the difference becomes greater between program yield versus expected yield.
 3. Have expectations of strong upward trend in corn prices to near \$3.00 neighborhood levels.
 4. Have a high risk preference and are "betting" on high yields and/or high corn prices.

B. Participation in Program by retiring 20% of corn base acreage and planting 80% of corn base acreage to corn.

1. Corn minimum price guarantee on all corn produced in the form of the loan provisions.
2. Income support from deficiency payments.
3. Cash flow benefits from advanced payments of 40% projected deficiency payment and the value of having that money in hand plus PIK Paid Land diversion.
4. Cash flow expenditures for variable cost are decreased because of the 20% reduction in acreage planted.
5. Established floor on price, but still retain the possible gains from price increase on bushels produced.
6. The question is: "Will the benefits gained from the guaranteed loan rate on the reduced bushels produced, the diversion payment and the deficiency payments exceed the profits foregone from the acreage removed from production."

C. Participation in Program at Reduced Corn Production Level.

1. If at least 40% of base acres are planted to corn and 18.6% are retired, up to the remaining 41.4% can be planted to a non-program crop. Non-program crops exclude barley, corn, cotton, oats, rice, sorghum, soybeans, and wheat.
2. Participants receive 92% of deficiency payment that could be received with maximum corn acreage (80% of base acres).

3. PIK Paid Land diversion payment is not changed.
4. Corn base acreage will not be reduced using this alternative.
5. The loan provides price risk production.
6. Cash flow expenditures for corn production are reduced.
7. Remember there is an 8% penalty in the deficiency payment for this alternative. The fewer acres of non-program crop planted, the fewer acres to split the penalty.
8. The question in addition to that raised in item B.6 above, is whether some non-program crops, e.g., vegetables, dry beans, alfalfa, can be produced that will yield a higher profit per acre as compared to corn with and without participation in the government program. **Remember that without a pricing contract for these non-program crops, you must bear the downside price risk that could occur with increased production of these crops. Corn producers participating in the program have a price floor or risk protection. Non-program crop producers on the open market have no protection from prices that could possibly go to zero.**

VI. Other Considerations

- Participation in the acreage reduction program would also result in lower use (employment) of own farm resources as labor and equity capital. Is there a positive opportunity cost for these resources, i.e., can the resources be profitably employed either on the farm or off the farm?
- "Use" of idled land--are there land improvement projects that can be accomplished during the time period of idleness, e.g., tile drainage, fencerow clearance, establishment of forage seeding, etc.?
- Crop rotation--"Will participation result in severe disturbance to agronomic crop rotation program OR, will participation result in crop yield benefits in subsequent years due to soil improvement, etc?"
- Pest control on idled acreages--does idle acreage permit a "free" opportunity to enhance control of problem pests, be it weeds, insects or diseases?
- There are long-run benefits to the corn production sector from high participation.

VII. Purpose of Worksheet and Example

- Attached is a blank worksheet plus one example to illustrate evaluation of three farm options: (1) No Participation; (2) Participation; (3) Participation with less than 80% of corn base planted to corn and producing non-program crops on remaining acreage.

- The method on the attached worksheet shows the gross margin (return to land, labor and equipment) of being in the program versus non-participation at an expected price. The example uses our expected prices and variable costs. For your evaluation, use your own expectations on yields, prices and variable costs as applied on your own base acreage and base yields.
- A critical question is: At what "expected" price should you sign up versus not signing up? This is called the "break-even" (B.E.) price. $B.E. = (\text{gross margin from being in the program} + \text{production expense if not in the program}) / \text{expected bushels to be produced (base acres times expected yield)}$. If you expect a price less than the B.E. price, participate. If you expect a higher price, you may not choose to participate. (See B.E. of \$2.78 in Example.)

VIII. Worksheet Guidelines

- A. Lines 1 through 9 of the worksheet present known data for the '86 program. These are the program numbers announced by the USDA and are needed to help calculate the expected returns of participating in the program. As can be seen each entry is numbered by line, these numbers are used in the worksheet to identify when the information on that line is used in the calculations.
- B. Lines 10 through 20 are the inputs to be entered by the individual farmer. Since each individual farm will have different figures for this section, it is important that you put in your numbers in order to have an accurate scenario. Again, each item has a line number to call for it when needed in the calculations.
- C. Lines 20 through 31 are used to calculate the revenue from each of three scenarios, non-participation, participation, and participation at lower corn acreage and having a non-program crop.

Some of the lines call for the entering of more data and other lines are used to make the necessary calculations given the inputted information. For example line 23 reads: ("23. Acres planted (line 10*line 22/100"). This line is used to calculate the number of acres actually planted to corn. To do this it calls for line 10, which is the program base acres, and multiplies it times line 22, which is the % of acres planted to corn, divided by 100. The division by 100 is needed to change the % to a decimal in order to do the calculation. The calculation needs to be done for each scenario as shown below:

$$\begin{aligned} \text{Not in acreage planted} &= 100 * 100/100 = 100 \text{ acres planted} \\ \text{Participation acreage planted} &= 100 * 80/100 = 80 \text{ acres planted} \\ \text{Participation Alt. acres corn} &= 100 * 40/100 = 40 \text{ corn acres planted} \end{aligned}$$

Note 1. In the example 40% of base acres is planted to corn and 41.4% to non-program crops. You can plant 40% to 80% corn and 0% to 41.4% non-program crops.

Note 2. Expected yields are requested on Line 21. You may desire to recognize that expected yield on the reduced acreage could be higher than expected yield on entire acreage. For example, you normally expected 100 bu/acre on your entire acreage. But the 20% you set aside only yields 80 bu/acre, what would be your expected yield on the remaining 80%? The calculation is below, but remember it is only as accurate as the numbers you put in.

$$\frac{\text{normal yield} - (\text{yield on diverted acres} * \% \text{ diverted})}{\% \text{ of base planted}} = \text{yield on actual planted}$$

$$\frac{100\text{bu/ac} - (80\text{bu/ac} * .20)}{.80} = 105 \text{ bu/ac}$$

Note 3. Line 29 asks for revenue from an alternative crop, here you must do the calculation of expected revenue per acre separately and enter it onto the worksheet, e.g., 13/cwt navybeans per acre times \$13/cwt equals \$169/acre.

- D. Lines 32 through 41 calculate the variable expenses. Here we are only interested in the expenses that change due to the planting of a particular crop. Ignore such costs as property taxes and machinery depreciation which do not change. Again, the expenses vary from farm to farm and you should use your own farm cost data. On line 38 of the example, the \$103 is our variable expense per acre for Navybeans.
- E. Line 42 gives you returns over variable costs. Here you subtract the variable expenses for each alternative, from its respective gross revenue. The result is the expected return to land, equipment, and management from each alternative. This is the critical line to be used in a farmers decision of whether or not to participate.
- F. The last section of the worksheet is designed to calculate your breakeven price. This should give you some sense regarding the possibility that your decision is not the most profitable choice.

8 EXAMPLE

WORKSHEET FOR EVALUATING THE 1986 CORN PROGRAM

PROGRAM KNOWN:

1. Target Price (\$/Bu)	\$3.03	6. % Advance Deficiency Payment	40.0 %
2. U.S. Loan Rate (\$/Bu)	\$1.92	7. % Advance Diversion Payment	0.0 %
3. Formula Loan Rate (\$/Bu)	\$2.40	8. % Deficiency Payment as PIK (is 25% of the 40% Advance Deficiency)	10.0 %
4. % Acreage Reduction Program	17.5 %	9. # Months, Advance Deficiency Payment Use	12.0
5. % Paid PIK Diversion	2.5 %		

FARM INPUTS:

10. Program Base Acres	<u>100</u> acres
11. Program Base Yield	<u>90</u> bu/acre
12. County Loan Rate	<u>\$ 1.92</u> /bu
13. Annual Interest Rate	<u>12</u> %
14. Expected U.S. Corn Price at Farm (Oct 86-Feb 87)	<u>\$ 1.95</u> /bu
15. Expected U.S. Corn Price at Farm (Oct 86-Sept 87)	<u>\$ 2.00</u> /bu
16. Expected Corn Price at your Farm (Oct 86 - Sept 87)	<u>\$ 2.00</u> /bu
17. USDA Expected Deficiency Payment per bushel	<u>\$ 1.03</u> /bu
18. Paid Land Diversion Payment rate per bushel	<u>\$.73</u> /bu
19. Months Corn Storage to Obtain Expected Price	<u>5.00</u> /mo
20. Expected Budget cuts due to Gramm-Rudmann Bill	4.3 %

REVENUE:

	NOT IN PROGRAM	IN PROGRAM	IN PROGRAM +ALT CROP
21. Expected Yield (Bu/Acre)	<u>100</u>	<u>105</u>	<u>105</u>
22. % Planted in Corn (>40% and < 80%) (for non-program alternative crop option)	100 %	80 %	<u>40</u>
23. Acres Planted (line 10*line 22/100)	<u>100</u>	<u>80</u>	<u>40</u>
24. Gross From Corn (line 16*21*23)	<u>\$ 2000.</u>	<u>\$ 16800.</u>	<u>\$ 8400.</u>
25. Deficiency Payment/Bu. (DP) If line 15 >\$3.03, DP=0 If line 15 < \$1.92, DP=\$1.11 If \$3.03 >line 15 >\$1.92, DP=\$3.03-line 15	\$0.00	<u>\$ 1.03</u>	<u>\$ 1.03</u>
26. Deficiency Payment for Farm (\$Cash+ PIK) (line 11*23*25)*(1-line 8/100)*(1-line 20/100) +(line 11*23*25)*(line 8/100) and times .92 for Alt. Crop Option	\$0.00	<u>\$ 7129.00</u>	<u>\$ 6503.68</u>
27. PIK Diversion Payment (line 10*11*18*.025)	\$0.00	<u>\$ 164.25</u>	<u>\$ 164.25</u>
28. Interest Earned on Advanced Deficiency (line 17*6*23*11)*(1-line 20/100) (line 13/12 mos. * line 9) and times .92 for Alt. Crop Option	\$0.00	<u>\$ 340.66</u>	<u>\$ 313.41</u>
29. Revenue Alternative Crop(s) (\$/Acre)	\$0.00	\$0.00	<u>\$ 169.00</u>
30. Gross Revenue Alternative Crop(s) (line 29 *(line 10 - line 23 - (line 10*.186))	\$0.00	\$0.00	<u>\$ 6996.60</u>
31. Gross Revenue from Corn Base Acreage (line 24+26+27+28+30)	<u>\$ 2000.00</u>	<u>\$ 24433.91</u>	<u>\$ 22432.94</u>

EXAMPLE

EXAMPLE

EXPENSES:

	NOT IN PROGRAM	IN PROGRAM	IN PROGRAM +ALT CROP
32. Variable Costs/acre	\$ <u>160.00</u>	\$ <u>160.00</u>	\$ <u>160.00</u>
33. Variable Costs for Corn (line 23*32)	\$ <u>16000.00</u>	\$ <u>12800.00</u>	\$ <u>6400.00</u>
34. Storage Costs/Bu/Month	\$ <u>.02</u>		
35. Storage Costs (Line*21*23*34) * line 19 or 9 months if in program and farm price loan rate	\$ <u>1000.00</u>	\$ <u>840.00</u>	\$ <u>420.00</u>
36. Cover Crop Costs/acre	\$0.00	\$ <u>10.00</u>	\$ <u>10.00</u>
37. Costs of Conserving Acres (line 36*10) *.20 or if Alt., then (Line 36*10) * .186	\$0.00	\$ <u>200.00</u>	\$ <u>186.00</u>
38. Variable Costs Alt. Crop(s)/acre	\$0.00	\$0.00	\$ <u>103.00</u>
39. Variable costs Alternative Crop(s) (line 38*(Line 10 - Line 23 - (Line 10*.186))	\$0.00	\$0.00	\$ <u>4264.20</u>
40. Interest on Expenses (line 33+37+39)* (line 13/12 mos.)*6 mos.	\$ <u>960.00</u>	\$ <u>780.00</u>	\$ <u>651.85</u>
41. Total Variable Expenses (line 33+35+37+39+40)	\$ <u>17960.00</u>	\$ <u>14620.</u>	\$ <u>11922.05</u>

NET REVENUE:

42. Gross Margin (line 31 - line 41)	\$ <u>2040.</u>	\$ <u>9813.91</u>	\$ <u>10510.89</u>
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BREAK-EVEN CORN PRICE

(Minimum corn price required to not participate)

$$\begin{aligned}
 &= \left[\begin{array}{c} \$ \text{Net Revenue} \\ \text{in program} \\ \text{(Line 42)} \end{array} \right] + \left[\begin{array}{c} \$ \text{Total Variable Expenses} \\ \text{Not in Program} \\ \text{(Line 41)} \end{array} \right] \div \left[\begin{array}{c} \text{Expected bushels to} \\ \text{be Produced if Not} \\ \text{in Program} \end{array} \right] \\
 \$ / \text{Bu Corn } 2.78 &= \left[\begin{array}{c} \$ \text{ 9813.91} \end{array} \right] + \left[\begin{array}{c} \$ \text{ 17960.} \end{array} \right] \div \left[\begin{array}{c} \text{ 10000.} \\ \text{bu} \end{array} \right]
 \end{aligned}$$

EXAMPLE

WORKSHEET FOR EVALUATING THE 1986 CORN PROGRAM**PROGRAM KNOWN:**

1. Target Price (\$/Bu)	\$3.03	6. % Advance Deficiency Payment	40.0 %
2. U.S. Loan Rate (\$/Bu)	\$1.92	7. % Advance Diversion Payment	0.0 %
3. Formula Loan Rate (\$/Bu)	\$2.40	8. % Deficiency Payment as PIK (is 25% of the 40% Advance Deficiency)	10.0 %
4. % Acreage Reduction Program	17.5 %	9. # Months, Advance Deficiency Payment Use	12.0
5. % Paid PIK Diversion	2.5 %		

FARM INPUTS:

10. Program Base Acres	_____	acres
11. Program Base Yield	_____	bu/acre
12. County Loan Rate	_____	/bu
13. Annual Interest Rate	_____	%
14. Expected U.S. Corn Price at Farm (Oct 86-Feb 87)	\$ _____	/bu
15. Expected U.S. Corn Price at Farm (Oct 86-Sept 87)	\$ _____	/bu
16. Expected Corn Price at your Farm (Oct 86 - Sept 87)	\$ _____	/bu
17. USDA Expected Deficiency Payment per bushel	\$ 1.03	/bu
18. Paid Land Diversion Payment rate per bushel	\$.73	/bu
19. Months Corn Storage to Obtain Expected Price	_____	/mo
20. Expected Budget cuts due to Gramm-Rudmann Bill	4.3	%

REVENUE:

	NOT IN PROGRAM	IN PROGRAM	IN PROGRAM +ALT CROP
21. Expected Yield (Bu/Acre)	_____	_____	_____
22. % Planted in Corn (>40% and < 80%) (for non-program alternative crop option)	100 %	80 %	_____
23. Acres Planted (line 10*line 22/100)	_____	_____	_____
24. Gross From Corn (line 16*21*23)	\$ _____	\$ _____	\$ _____
25. Deficiency Payment/Bu. (DP) If line 15 > \$3.03, DP=0 If line 15 < \$1.92, DP=\$1.11 If \$3.03 > line 15 > \$1.92, DP=\$3.03-line 15	\$0.00	\$ _____	\$ _____
26. Deficiency Payment for Farm (\$Cash+ PIK) (line 11*23*25)*(1-line 8/100)*(1-line 20/100) +(line 11*23*25)*(line 8/100) and times .92 for Alt. Crop Option	\$0.00	\$ _____	\$ _____
27. PIK Diversion Payment (line 10*11*18*.025)	\$0.00	\$ _____	\$ _____
28. Interest Earned on Advanced Deficiency (line 17*6*23*11)*(1-line 20/100) (line 13/12 mos. * line 9) and times .92 for Alt. Crop Option	\$0.00	\$ _____	\$ _____
29. Revenue Alternative Crop(s) (\$/Acre)	\$0.00	\$0.00	\$ _____
30. Gross Revenue Alternative Crop(s) (line 29 *(line 10 - line 23 - (line 10*.186))	\$0.00	\$0.00	\$ _____
31. Gross Revenue from Corn Base Acreage (line 24+26+27+28+30)	\$ _____	\$ _____	\$ _____

EXPENSES:

	NOT IN PROGRAM	IN PROGRAM	IN PROGRAM +ALT CROP
32. Variable Costs/acre	\$ _____	\$ _____	\$ _____
33. Variable Costs for Corn (line 23*32)	\$ _____	\$ _____	\$ _____
34. Storage Costs/Bu/Month	\$ _____		
35. Storage Costs (Line*21*23*34) * line 19 or 9 months if in program and farm price loan rate	\$ _____	\$ _____	\$ _____
36. Cover Crop Costs/acre	\$0.00	\$ _____	\$ _____
37. Costs of Conserving Acres (line 36*10) *.20 or if Alt., then (Line 36*10) * .186	\$0.00	\$ _____	\$ _____
38. Variable Costs Alt. Crop(s)/acre	\$0.00	\$0.00	\$ _____
39. Variable costs Alternative Crop(s) (line 38*(Line 10 - Line 23 - (Line 10*.186))	\$0.00	\$0.00	\$ _____
40. Interest on Expenses (line 33+37+39)* (line 13/12 mos.)*6 mos.	\$ _____	\$ _____	\$ _____
41. Total Variable Expenses (line 33+35+37+39+40)	\$ _____	\$ _____	\$ _____

NET REVENUE:

42. Gross Margin (line 31 - line 41)	\$ _____	\$ _____	\$ _____
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BREAK-EVEN CORN PRICE

(Minimum corn price required to not participate)

$$= \left[\frac{\$ \text{Net Revenue in program (Line 42)}}{\$} \right] + \left[\frac{\$ \text{Total Variable Expenses Not in Program (Line 41)}}{\$} \right] \div \left[\frac{\text{Expected bushels to be Produced if Not in Program}}{\text{bu}} \right]$$

\$ /Bu Corn