farmdoc
decision · outreach · central

Improving farm decision-making under risk through education and research.

Agricultural Law, Taxation & Policy: Key Issues and Developments

By D. Uchtmann & B. Endres, Gary Hoff, and Bob Hauser

Presented at the Farm Income 2004 Programs

1867

http://www.farmdoc.uiuc.edu/

Agricultural Law Topics

- Changes in the IL Grain Code
- Liability Issues in Growing Tx Crops
- Non-StarLink Farmer Litigation

Presented by

Don Uchtmann & Bryan Endres

Professor & Asst. Professor

of Agricultural Law

Background: IL Grain Code Created The IL Grain Insurance Fund
(FDIC Analogy)

FDIC: deposits of money are insured if the member bank fails

IGIF: grain deposits (and qualifying grain sales if seller unpaid) insured if IL-licensed elevator fails

IL Grain Code Changes

- The amendment gives more protection to farmers in the event of IL grain dealer or warehouse failure,
- But the added protection comes at a cost.

Increased Farmer Protection

(Lessons from Ty-Walk)

- Size of IGIF: \$3 Mil. → \$6 Mil.
- Some important changes:
  - Higher Payment Limits for claims paid at 85%, i.e., \$100,000 limit → \$250,000 limit
  - Price Later Contracts covered for longer time, i.e., 270 day max → 365 day max (after later of date of contract or date of delivery)
- See Checklist of "good practices" for farmers

Greater Protection Through Increased Oversight

- Oversight of "farmer marketing programs" by the IDOA clarified/expanded
- Riskiness of marketing programs offered → Intensity of annual examination by IDOA

Three Levels of Examination

Minimal market risk →

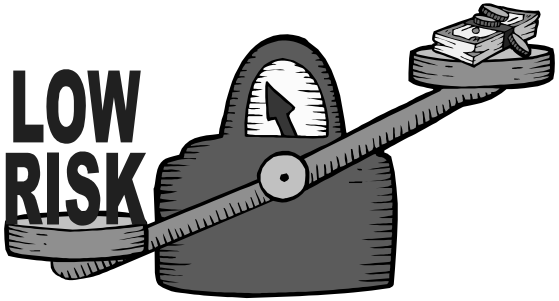
Basic Examination

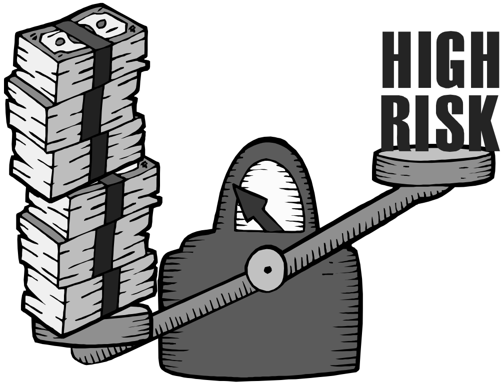
Increased risk →

Intermediate Exam

The most risk →

Advanced Exam





Skip to Slide 12, P. 124 (Bottom)

If Licensee . . .

- Has discretionary trading authority from producers,
- Uses "premium offer" type contracts, or
- Has contracts with producers that cover multiple crop years

Then exam includes:

- Everything done if low or middle risk,
- Evaluation of market risk exposure and use of appropriate risk management tools, and
- Adequacy of internal controls

Outside Experts/Regulatory Fund

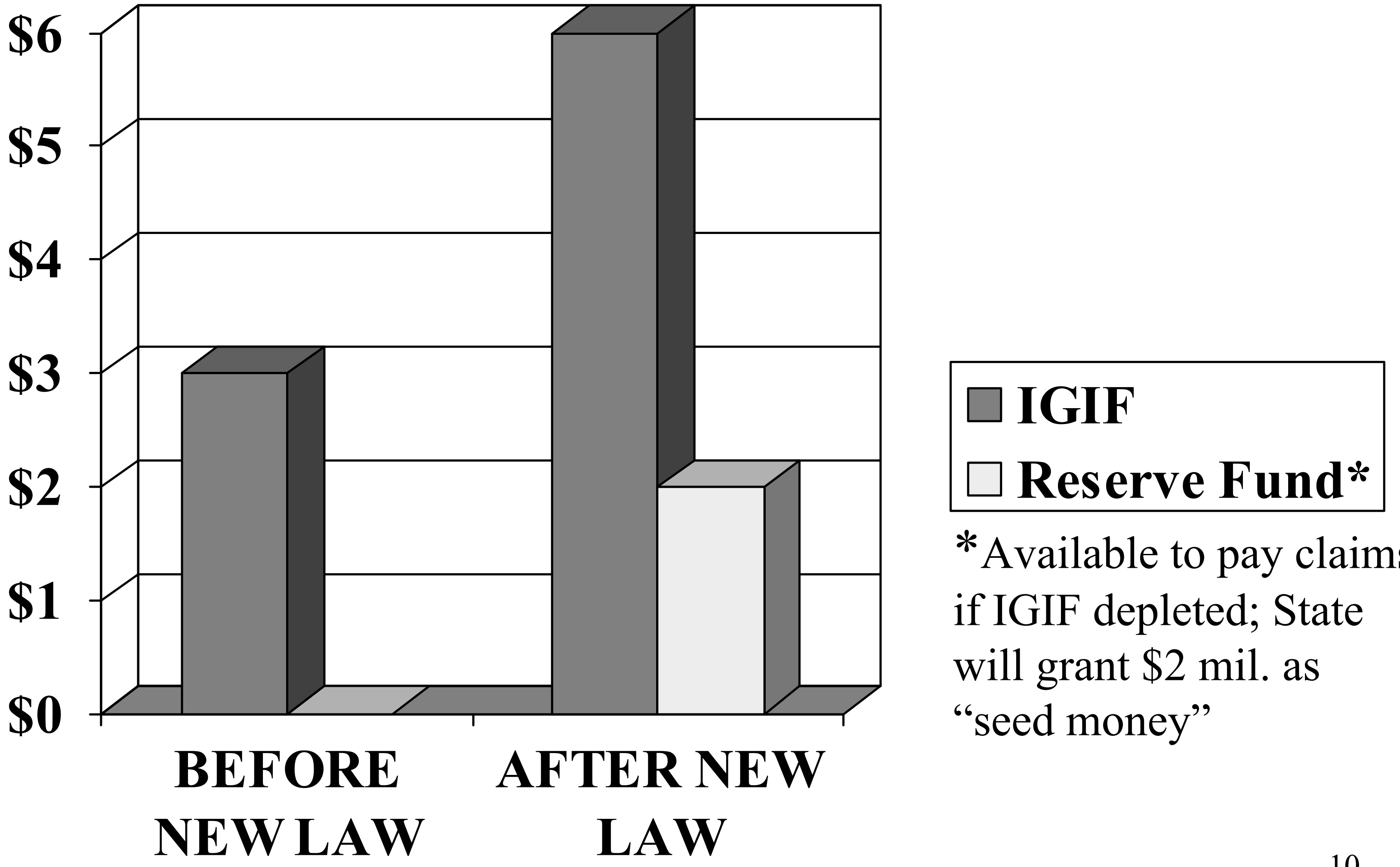
For Intermediate or Advanced Examinations:

- Department is authorized to engage
  - Outside accounting experts, and
  - Grain risk management experts
- Regulatory Fund may be tapped to pay for these outside experts
- New Regulatory Fund is funded by, e.g.,

  (a) Increases in license application fees ($50 increase) and annual license renewal fees ($100 increase), and

  (b) Fees for each required certificate. 240 ILCS 40/35-5

Greater Protection: Reserve Fund



*Available to pay claims if IGIF depleted; State will grant $2 mil. as "seed money"

Reserve Fund (New § 30-25)

- History: IGIF borrowed $4 mil. from State to pay obligations created by Ty-Walk failure
- New Law: When loan repaid, State pays $2 mil.
  - Seed money for Reserve Fund
- This "Reserve Fund" used to pay claims when IGIF insufficient
- Reserve Fund replenished with, e.g., IGIF assessments
- Good News: Income from Reserve Fund to IGIF

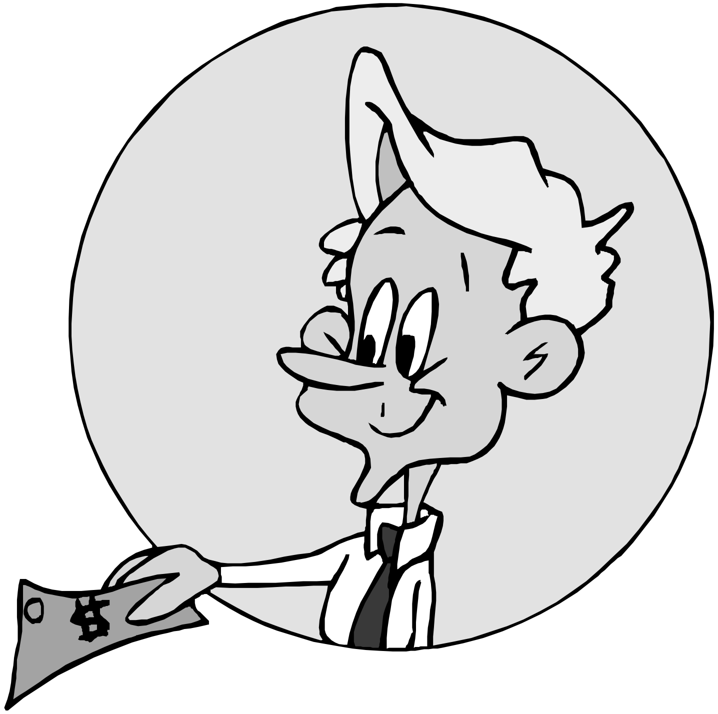
Summary of Added Protection

- More Resources available to pay claims
  - $6 mil IGIF (when Fund "recharged")
  - $2 mil Reserve Fund (when loan repaid)
- More Producer Claims eligible for payment
  - **$250,000** limit for Claims paid @ 85%
  - Price Later Contracts "covered" for **365** days
  - **Clarification** of some rules, e.g., 160-day rule
- Greater Department Oversight of Farmer Marketing Programs, etc.

The Added IGIF Protection Comes At a Price

Beginning in January 2004, 1st sellers of grain will pay IGIF Assessments . . .

- for the 1st time,
- when they "settle for" grain sold to an IL-licensed facility



Assessments on 1st Sellers

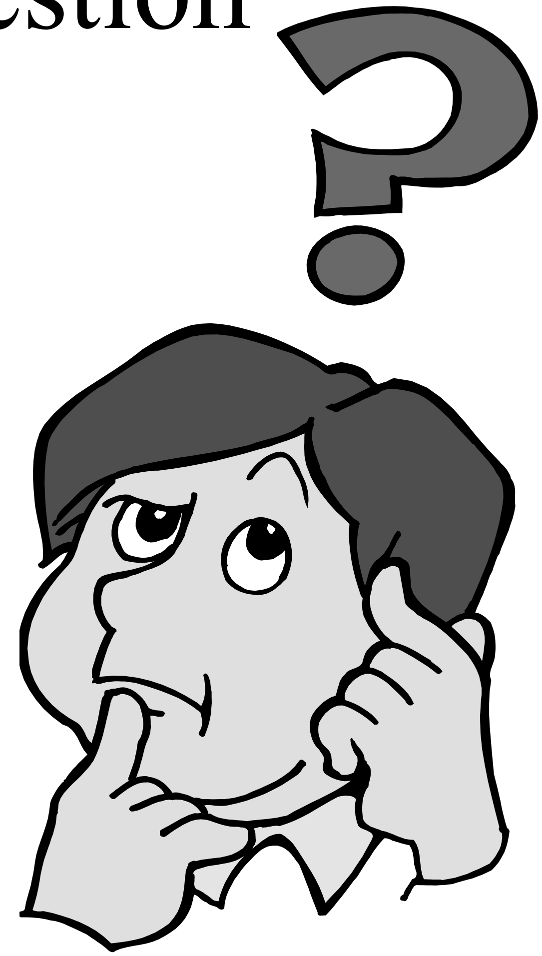
- Rate: 0.0004
  - I.e., $4 for each $10,000 of grain "settled for"
- Mechanics:
  - Grain dealer collects assessment at settlement
  - Remits the assessment quarterly to the Ill. Department of Agriculture
- Assessment Cycle:
  - 12 Months "On" and 6 months "Off"

12 Months "On" – 6 Months "Off" IGIF Assessment Cycle

2004	2005	2006
Jan – Mar	Jan – Mar (off)	Jan - Mar
April - Jun	April – Jun (off)	April - Jun
July - Sept	July - Sept	July – Sept (off)
Oct - Dec	Oct - Dec	Oct – Dec (off)

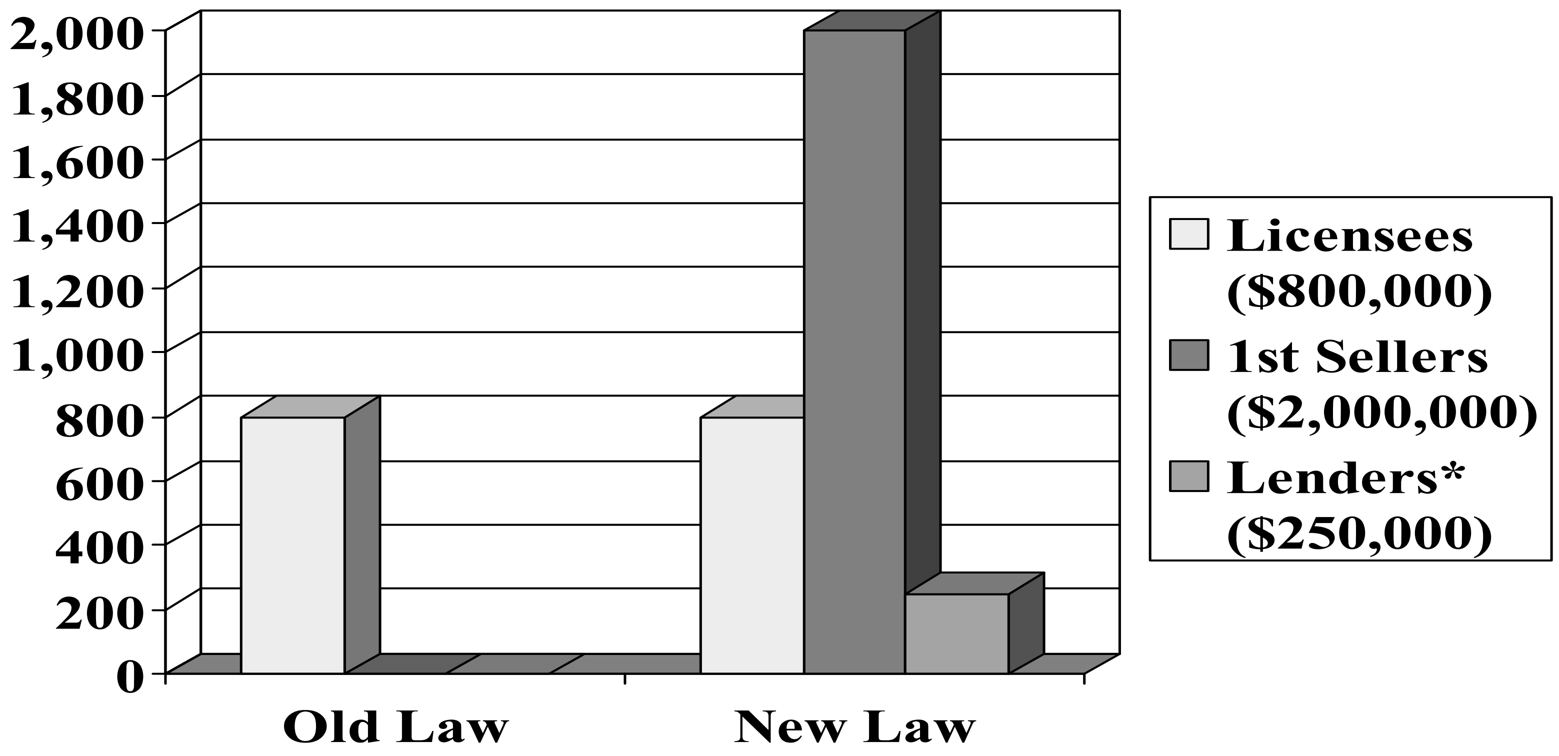
Marketing Question

- Will the assessment of $4 per $10,000 of grain “settled for” after December 31 cause you to “settle” for sales before January 1?



Estimated Dollars Raised for IGIF

Per Assessment Cycle (in $1000s)



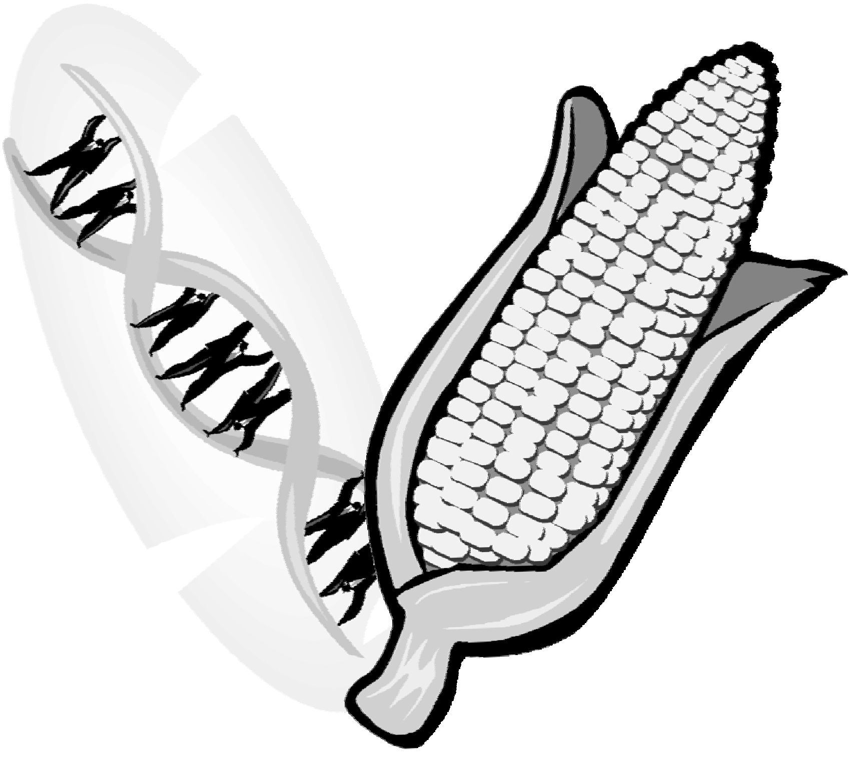
**Lenders holding warehouse receipts to secure loans to licensees also pay assessments for the 1st time starting January 2004*

Policy Issue: Are Farmers Paying Too Much?

- $2,000,000 *v.* $800,000 or $250,000?
- Relatively high burden per assessment cycle <u>mitigated</u> by FEWER cycles
- See supplemental handout
  - Farmers pay until IGIF hits $3,000,000
  - Elevators, Bankers pay if < $6,000,000
- IL: $2 mil. to "seed" Reserve Fund

Liability Issues When Growing Tx Crops

- What are the liability Risks?
- What actions might reduce these risks?



E.g., Rootworm Resistant Corn

- YieldGuard Rootworm Bt corn may be a popular planting choice next Spring
- It is approved for use in the USA, but not in European Union
- Pollen could drift to the fields of a neighbor who sells corn to buyers that do not accept "unapproved in EU" corn varieties
- Who would be liable for what?

Liability Risks

- Applicable law is not well-developed, but we can probably say . . .
- Farmer v. Farmer suits for economic losses arising from Tx pollen drift are not likely to be successful, absent new developments in the law,

  PROVIDED . . .

<u>Probably</u> no liability *provided*:

- Farmer fulfills all required conditions on the label and licensing agreement,
- Tx crop grown in accordance with any state or local laws regarding such crops (no special rules under IL law), and
- Intentional conduct (e.g. Hatfield v. McCoy)

Caveat: Legal theories that *might* support plaintiff's case do exist

For Example . . .

- Trespass
- Nuisance
- Negligence
- Others

Possible Risk-reducing steps:

Farmer gives *notice*, i.e., tells neighbors who sell into export channels (and who ask?)

(1) that Farmer is growing a variety not approved in overseas markets, and

(2) where it will be planted

And . . .

Potential steps, *cont'd*

Farmer exercises ***reasonable care*** to minimize the likelihood of pollen drift problems, e.g.,

- Maybe Farmer plants part of the 20% non-Bt refuge area as a buffer <u>between</u> his fields containing "unapproved in EU" varieties *and* Neighbor's "bound for export" fields?
- This way, the refuge also acts as a pollen-catching buffer between Farmer's crop and the crop of his neighbor?

What is "reasonable care" in this kind of setting?

- What should a "reasonable farmer" do to prevent "unreasonable harm" to a neighbor?
- What do you think??

The “Flipside” of this Issue

What about Farmers signing “No-GMO” contracts (contracts that guarantee the genetic “purity” of the crop to be sold)?

Signing Contracts, *Cont'd*

The farmers are . . .

1. Contractually assuming a liability risk beyond their control, e.g.,
   - Pollen may drift into Farmer's fields, or
   - Seed may not be "genetically pure"
2. Limited in their ability to pass on their contractually-created liability to the neighbor from whom pollen may have drifted

NON-STARLINK FARMER LITIGATION
NON-STARLINKFARMERSSETTLEMENT.COM

What happened in this class action?

Plaintiffs' Argument: The presence of StarLink in the year 2000 corn crop depressed the price of US corn, causing damage to all producers who sold corn.

farmdoc

NON-STARLINK FARMER LITIGATION

NON-STARLINKFARMERSSETTLEMENT.COM

Court Approved Settlement:

Defendants pay $110 million + interest

Court costs, attorney's fees, etc. paid 1st

Property Damage claims paid 2nd

Corn Loss claims paid 3rd (out of residue)

NON-STARLINK FARMER LITIGATION

NON-STARLINKFARMERSSETTLEMENT.COM

"Corn Loss" Claims:

- Proof of Claim due 7/31/03
- "Notice of Problem" sent to some farmers 10/15/03
- Most Responses due 11/15/03

What was your experience????

Corn Loss Payments:

- When coming?
- Amount?
- Form of Payment?
- Must Producer account to others?
- Who pays the taxes?

Jobs and Growth Tax Relief Reconciliation Act of 2003

By Gary Hoff
Extension Tax Specialist

Taxation Subtopics:

- Increased Depreciation
- Tax Planning
- Capital Gains and Losses
- Dividends
- Estate and Gift Taxes

Justice Learned Hand:

"There are two systems of taxation in our country: one for the informed, and one for the uninformed.

“Over and over again Courts have said there is nothing sinister in so arranging one's affairs as to keep taxes as low as possible.

“Everybody does so, rich and poor, and all do right, for nobody owes any public duty to pay more than the law demands.

“Taxes are enforced exactions, not voluntary contributions. To demand more in the name of morals is mere cant [moralizing].

Boom or Boondoggle

- May save substantial tax.
- Immediate savings.
- Less regular tax

- Much of savings is only a postponement.
- Ends on 1/1/2005.
- May create AMT

INCREASED DEPRECIATION

New Combine

- Purchase after 5/6/2003
- Cost $233,500

Old Law

SCHEDULE F (Form 1040) — Department of the Treasury, Internal Revenue Service (99)

Profit or Loss From Farming

► Attach to Form 1040, Form 1041, Form 1065, or Form 1065-B.

► See Instructions for Schedule F (Form 1040).

OMB No. 1545-0074 — 2003 — Attachment Sequence No. 14

Name of proprietor | Social security number (SSN)

A Principal product. Describe in one or two words your principal crop or activity for the current tax year. | B Enter code from Part IV

C Accounting method: (1) ☐ Cash (2) ☐ Accrual | D Employer ID number (EIN), if any

E Did you "materially participate" in the operation of this business during 2003? If "No," see page F-2 for limit on passive losses. ☐ Yes ☐ No

Part I Farm Income—Cash Method. Complete Parts I and II (Accrual method taxpayers complete Parts II and III, and line 11 of Part I.)
Do not include sales of livestock held for draft, breeding, sport, or dairy purposes; report these sales on Form 4797.

1 Sales of livestock and other items you bought for resale — 1
2 Cost or other basis of livestock and other items reported on line 1 — 2
3 Subtract line 2 from line 1 — 3
4 Sales of livestock, produce, grains, and other products you raised — 4
5a Total cooperative distributions (Form(s) 1099-PATR) 5a — 5b Taxable amount — 5b
6a Agricultural program payments (see page F-2) 6a — 6b Taxable amount — 6b
7 Commodity Credit Corporation (CCC) loans (see page F-3):
a CCC loans reported under election — 7a
b CCC loans forfeited 7b — 7c Taxable amount — 7c
8 Crop insurance proceeds and certain disaster payments (see page F-3):
a Amount received in 2003 8a — 8b Taxable amount — 8b
c If election to defer to 2004 is attached, check here ► ☐ — 8d Amount deferred from 2002 — 8d
9 Custom hire (machine work) income — 9
10 Other income, including Federal and state gasoline or fuel tax credit or refund (see page F-3) — 10
11 **Gross income.** Add amounts in the right column for lines 3 through 10. If accrual method taxpayer, enter the amount from page 2, line 51 ► — 11

Part II Farm Expenses—Cash and Accrual Method. Do not include personal or living expenses such as taxes, insurance, repairs, etc., on your home.

12 Car and truck expenses (see page F-4—also attach **Form 4562**) — 12
13 Chemicals — 13
14 Conservation expenses (see page F-4) — 14
15 Custom hire (machine work) — 15
16 Depreciation and section 179 expense deduction not claimed elsewhere (see page F-4) — 16
17 Employee benefit programs other than on line 25 — 17
18 Feed purchased — 18
19 Fertilizers and lime — 19
20 Freight and trucking — 20
21 Gasoline, fuel, and oil — 21
22 Insurance (other than health) — 22
23 Interest:
a Mortgage (paid to banks, etc.) — 23a
b Other — 23b
24 Labor hired (less employment credits) — 24
25 Pension and profit-sharing plans — 25
26 Rent or lease (see page F-5):
a Vehicles, machinery, and equipment — 26a
b Other (land, animals, etc.) — 26b
27 Repairs and maintenance — 27
28 Seeds and plants purchased — 28
29 Storage and warehousing — 29
30 Supplies purchased — 30
31 Taxes — 31
32 Utilities — 32
33 Veterinary, breeding, and medicine — 33
34 Other expenses (specify): a — 34a; b — 34b; c — 34c; d — 34d; e — 34e; f — 34f

35 **Total expenses.** Add lines 12 through 34f ► — 35
36 **Net farm profit or (loss).** Subtract line 35 from line 11. If a profit, enter on **Form 1040, line 18**, and **also** on **Schedule SE, line 1.** If a loss, you **must** go on to line 37 (estates, trusts, and partnerships, see page F-6) — 36
37 If you have a loss, you **must** check the box that describes your investment in this activity (see page F-6).
• If you checked 37a, enter the loss on **Form 1040, line 18,** and **also** on **Schedule SE, line 1.**
• If you checked 37b, you **must** attach **Form 6198.**
37a ☐ All investment is at risk.
37b ☐ Some investment is not at risk.

For Paperwork Reduction Act Notice, see Form 1040 instructions. Cat. No. 11346H **Schedule F (Form 1040) 2003**

Draft as of 5/30/2003

20%

$47,339

New law

SCHEDULE F (Form 1040)
Department of the Treasury Internal Revenue Service (99)

Profit or Loss From Farming
► Attach to Form 1040, Form 1041, Form 1065, or Form 1065-B.
► See Instructions for Schedule F (Form 1040).

OMB No. 1545-0074 **2003** Attachment Sequence No. **14**

Draft as of 5/30/2003

Name of proprietor | Social security number (SSN)

A Principal product. Describe in one or two words your principal crop or activity for the current tax year. | B Enter code from Part IV ►

C Accounting method: (1) ☐ Cash (2) ☐ Accrual | D Employer ID number (EIN), if any

E Did you "materially participate" in the operation of this business during 2003? If "No," see page F-2 for limit on passive losses. ☐ Yes ☐ No

Part I Farm Income—Cash Method. Complete Parts I and II (Accrual method taxpayers complete Parts II and III, and line 11 of Part I.)
Do not include sales of livestock held for draft, breeding, sport, or dairy purposes; report these sales on Form 4797.

1 Sales of livestock and other items you bought for resale . . . 1
2 Cost or other basis of livestock and other items reported on line 1 . . . 2
3 Subtract line 2 from line 1 . . . 3
4 Sales of livestock, produce, grains, and other products you raised . . . 4
5a Total cooperative distributions (Form(s) 1099-PATR) 5a | 5b Taxable amount 5b
6a Agricultural program payments (see page F-2) 6a | 6b Taxable amount 6b
7 Commodity Credit Corporation (CCC) loans (see page F-3):
a CCC loans reported under election . . . 7a
b CCC loans forfeited . . . 7b | 7c Taxable amount 7c
8 Crop insurance proceeds and certain disaster payments (see page F-3):
a Amount received in 2003 . . . 8a | 8b Taxable amount 8b
c If election to defer to 2004 is attached, check here ► ☐ | 8d Amount deferred from 2002 . . 8d
9 Custom hire (machine work) income . . . 9
10 Other income, including Federal and state gasoline or fuel tax credit or refund (see page F-3) . . . 10
11 **Gross income.** Add amounts in the right column for lines 3 through 10. If accrual method taxpayer, enter the amount from page 2, line 51 . . . ► 11

Part II Farm Expenses—Cash and Accrual Method. Do not include personal or living expenses such as taxes, insurance, repairs, etc., on your home.

12 Car and truck expenses (see page F-4—also attach **Form 4562**)	12	25 Pension and profit-sharing plans	25
13 Chemicals	13	26 Rent or lease (see page F-5):	
14 Conservation expenses (see page F-4)	14	a Vehicles, machinery, and equipment	26a
15 Custom hire (machine work)	15	b Other (land, animals, etc.)	26b
16 Depreciation and section 179 expense deduction not claimed elsewhere (see page F-4)	16	27 Repairs and maintenance	27
		28 Seeds and plants purchased	28
		29 Storage and warehousing	29
17 Employee benefit programs other than on line 25	17	30 Supplies purchased	30
		31 Taxes	31
18 Feed purchased	18	32 Utilities	32
19 Fertilizers and lime	19	33 Veterinary, breeding, and medicine	33
20 Freight and trucking	20	34 Other expenses (specify):	
21 Gasoline, fuel, and oil	21	a	34a
22 Insurance (other than health)	22	b	34b
23 Interest:		c	34c
a Mortgage (paid to banks, etc.)	23a	d	34d
b Other	23b	e	34e
24 Labor hired (less employment credits)	24	f	34f

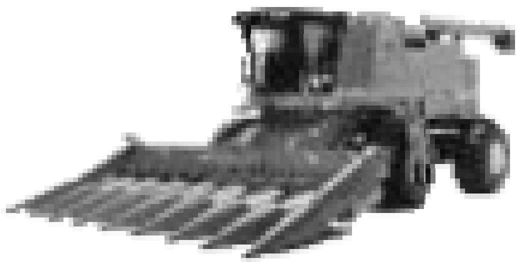
78%

35 **Total expenses.** Add lines 12 through 34f . . . 35
36 **Net farm profit or (loss).** Subtract line 35 from line 11. If a profit, enter on **Form 1040, line 18**, and also on **Schedule SE, line 1.** If a loss, you must go on to line 37 (estates, trusts, and partnerships, see page F-6) . . . 36

$181,054

37 If you have a loss, you **must** check the box that describes your investment in this activity (see page F-6).
• If you checked 37a, enter the loss on **Form 1040, line 18,** and also on **Schedule SE, line 1.**
• If you checked 37b, you **must** attach **Form 6198.**
37a ☐ All investment is at risk.
37b ☐ Some investment is not at risk.

For Paperwork Reduction Act Notice, see Form 1040 instructions. Cat. No. 11346H **Schedule F (Form 1040) 2003**



WHAT CHANGED?

- 30%/50% bonus depreciation
- IRC §179 deduction (1st year)

50% bonus IF

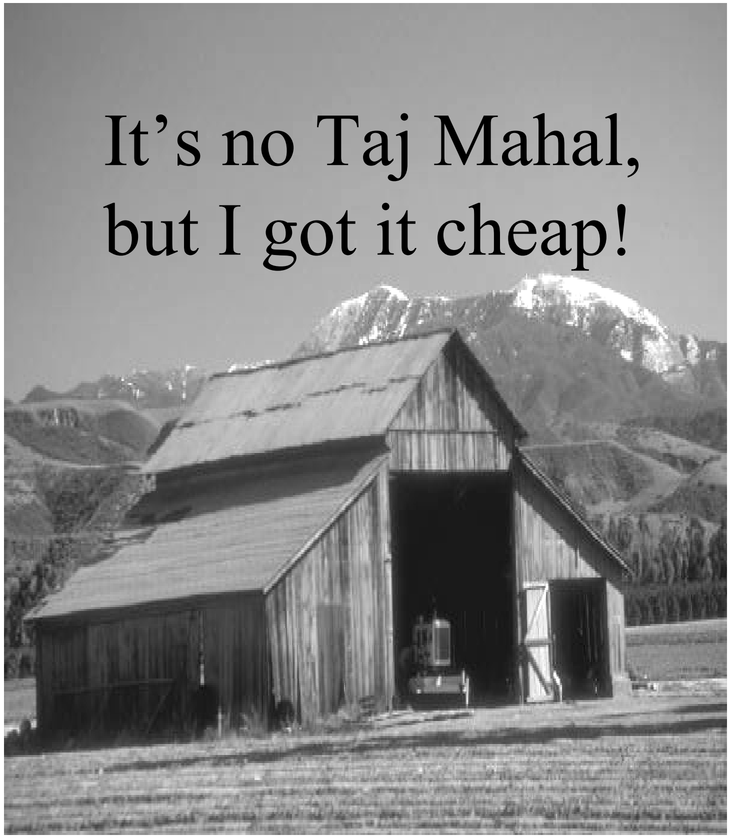
- New original use property
- Acquired after May 5, 2003
- Acquired before January 1, 2005
- 3, 5, 7, 10, 15, or 20-year property

EXAMPLES

Purchase	Acquired	N or U	Eligible
SUV	5/1/2003	N	No
Tractor	6/10/2003	U	No
Grain Dryer	8/1/2003	N	Yes
Rental House	7/1/2003	N	No

Machinery Shed

- Acquired February 5, 1965
- Remodeled on October 4, 2003
- Remodeling cost $40,000
- Only the $40,000 is available for 50%



Used Grain Bin

- Acquired from neighbor August 7, 2003
- Paid $5,000
- Cost $3,000 to move
- Only $3,000 is available for 50%

CAUTION

- All or nothing in a class
- Mandatory unless elect out
  - Can create depreciation allowed or allowable problem.
- Use of 50% will exempt the depreciation from AMT.

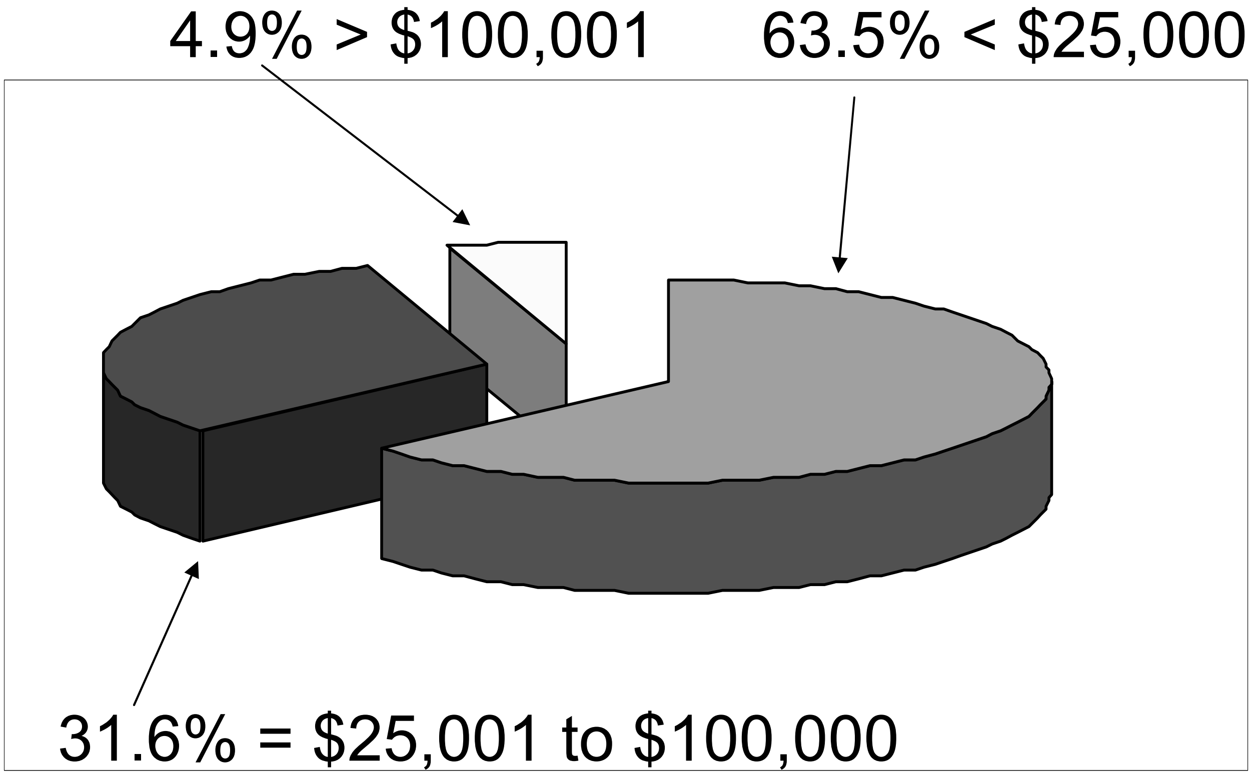
Section 179

- Up to $100,000 per year.
  - Down to $25,000 in 2006
- Phase-out at $400,000
- **New or used**
- **Tangible personal property** used in an
- **Active trade or business**

EXAMPLE

2003 eligible purchases	$425,000
Limit	400,000
Overage	$25,000
Maximum 179 deduction	$100,000
Reduction	25,000
179 deduction allowed	$75,000

2002 PURCHASES
4,074 ILLINOIS FARMERS



TRACTOR TRADE

- Initial purchase in 2000 of $100,000
- Trade in 2001 for $25,000 boot
- Trade again in 2002 for $25,000 boot
- Trade after 5/6/2003 for $25,000 boot

2003 Depreciation

Treasury Decision 9091

Cash Outlay
$25,000

Before
$46,647

After
$66,014

NOTICE 2000-4

- Like-kind exchange
- Continue depreciating the unrecovered cost of the old asset using its original life and method

TRACTOR TRADE

- Initial purchase in 2000 of $100,000
- Trade in 2001 for $25,000 boot
- Trade again in 2002 for $25,000 boot
- Trade after 5/6/2003 for $25,000 boot

Before 2003 depreciation, basis was $105,466

TAX PLANNING

BENEFIT OF CONSISTENT INCOME

- 14 year period
- $10,000 taxable income one year
- $120,000 taxable income next year
- $173,464 total tax

BENEFIT OF CONSISTENT INCOME

- 14 year period
- $65,000 taxable income each year
- $138,180 total tax

BENEFIT OF CONSISTENT INCOME

- Consistent income saved $35,284.
- Because of increasing marginal rate

Married Filing Jointly

If taxable income is

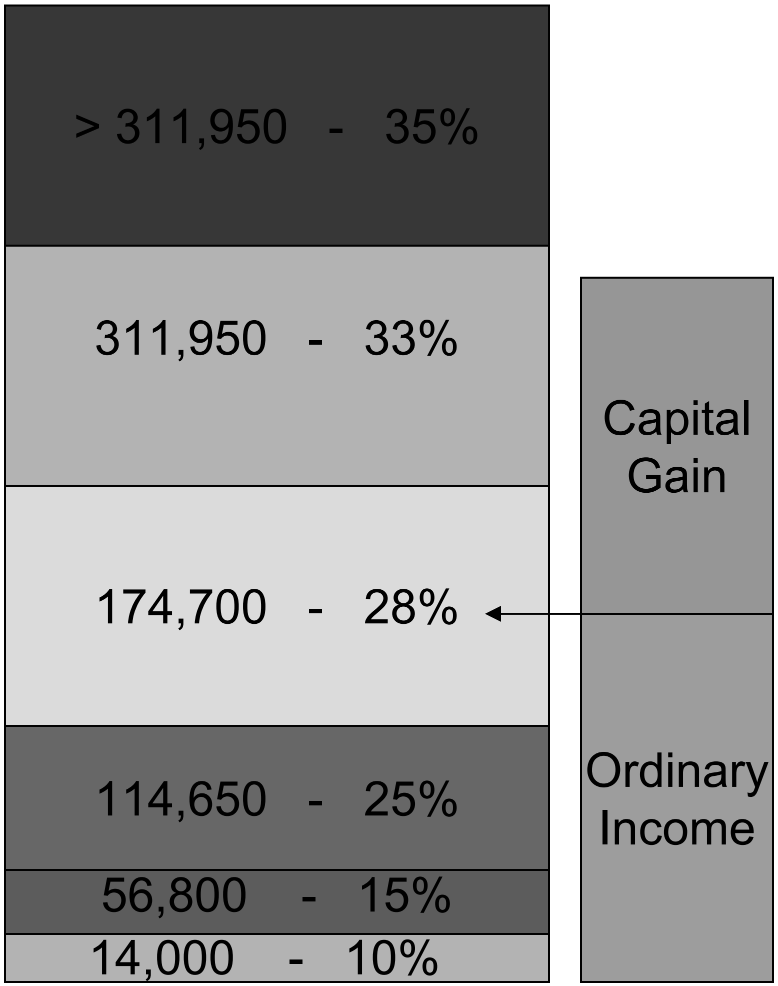
Over	But not over	The tax is	Plus	Of the amount over
0	14,000	0	10.0%	0
14,000	56,800	1,400	15.0%	14,000
56,800	114,650	7,820	25.0%	56,800
114,650	174,700	22,283	28.0%	114,650
174,700	311,950	39,097	33.0%	174,700
311,950		84,389	35.0%	311,950

LONG-TERM CAPITAL GAINS

CHANGE

- If in 10% or 15% marginal tax bracket, capital gains taxed at 5%.
- If in 25% or greater marginal tax bracket, capital gains taxed at 15%.
- Under old law capital gain rates were 8% and 20%.
- No change in capital loss rules.

Married Filing Joint



IF . .

Taxable income $310,000

Capital gain 150,000

THEN . . .

$ 14,000 taxed at 10%

$ 42,800 taxed at 15%

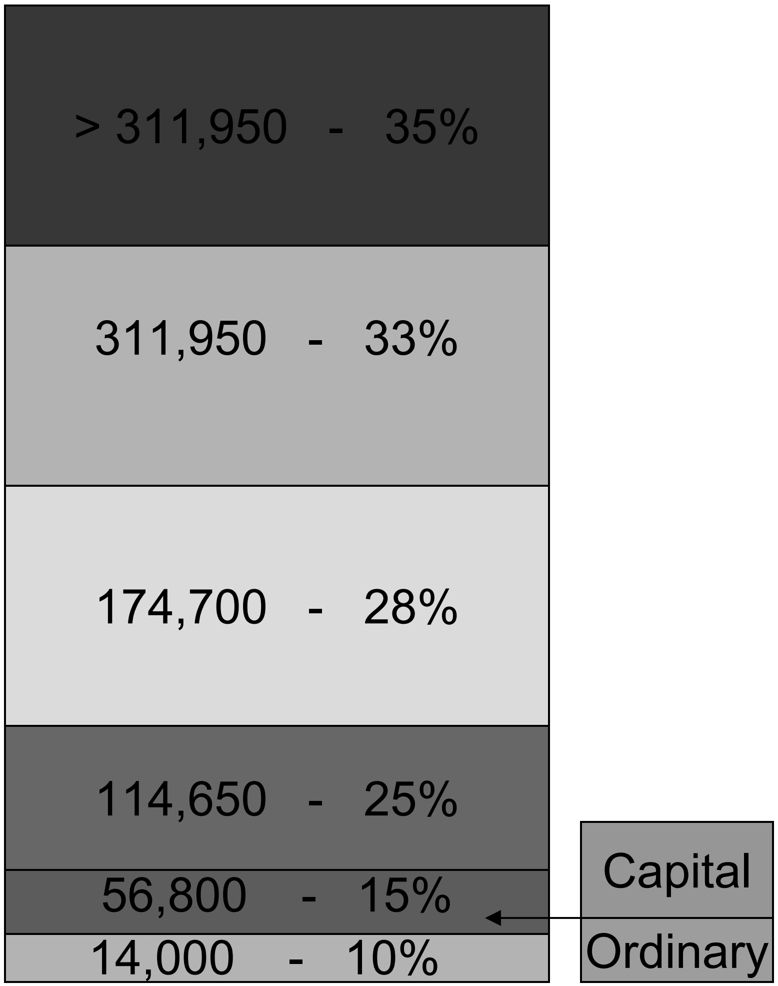
$ 57,850 taxed at 25%

$ 45,350 taxed at 28%

$150,000 taxed at 15%

Plus AMT

Married Filing Joint



IF

Taxable income $65,000
Capital gain 40,000

THEN

$14,000 taxed at 10%
$11,000 taxed at 15%
$31,800 taxed at 5%
$ 8,200 taxed at 15%

Eligibility Rules

- Sale or payment received after 5/5/2003.
- Sunset date of 12/31/2008.
- For sales between 1/1/2008 and 12/31/2008, the 5% rate goes to 0%

QUESTIONS

- Should I sell or use a §1031 exchange?
  - Basis issue
  - Management issue

DIVIDENDS

OLD RULES

- Double taxation.
- Taxed as ordinary income.

NEW RULES

- Double taxation.
- Taxed same as capital gain.
- Effective for dividends received after 12/31/2002.
- 60 day holding period.
- Sunset 12/31/2008.

QUESTIONS

- Should I pay dividends from my closely held corporation?
- Should I move my investments to stocks paying high dividends?

EXAMPLE

- Microsoft has $43 billion cash.
- Gates owns 1.2 billion shares.
- Paid 8¢ dividend.
- Received $99.5 million.
- Saved $19.5 million of tax.

ESTATE TAXES

For estates

Over	But not over	The tax is	Plus	Of the amount over
1,250,000	1,500,000	448,300	43%	1,250,000
1,500,000	2,000,000	555,800	45%	1,500,000
2,000,000	2,500,000	780,800	49%	2,000,000
2,500,000		1,025,800	50%	2,500,000

UNIFIED CREDIT

Year	Credit Amount	Exclusion Amount
2003	$345,800	$1,000,000
2004 – 2005	555,800	1,500,000
2006 – 2008	780,800	2,000,000
2009	1,455,800	3,500,000
2010	REPEALED	
2011	345,800	1,000,000

GIFTING

- Frozen at $1,000,000.
- $11,000/year.

REVIEW ESTATE PLAN

- Based on gifting assets such as units of FLP of shares of LLC.

OLDER FLP'S

- Donor maintains control.
  - Sell at a discount.
  - Take money over time.
- Donor keeps income.
  - Little or no distributions to limited partners.
  - Donor takes unlimited distributions.

RECENT CASES

- M.B. Harper Est.; TC Memo 2002-121
- T.R. Thompson Est.; TC Memo 2002-246
- D.A. Kimbell, Sr. Est.; 2003-1 USTC ¶60,455
- A. Strangi Est.; TC Memo 2003-145
- Hackl, Sr; 7th Cir Ct of Appeals 2003-2

Harper

- Formed FLP 6/14/94, died 2/1/95
- Son .4% GP was manager
- Transferred 60% to children
- FLP primarily owned securities.
- Distributions weighted heavily to Harper.

Thompson

- Formed 2 FLP's 2 years before death.
  - One for son
  - One for daughter
- GP was a corporation with Thompson owning 49%.
- Son had contributed substantial assets.
- Letters from advisors shown in court.
- Distributions primarily to Thompson.

Kimbell

- FLP formed 2 months prior to death.
- Kimbell held 99% of LP interest.
- Kimbell held 50% of LLC that was manager of FLP

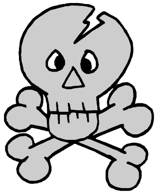
Strangi

- Formed just prior to death.
- Son-in-law had POA and formed FLP.
- Corporate GP with Strangi owning 47%.
- (*% of Strangi's assets transferred with Strangi owning 99% of LP units.
- FLP paid all of Strangi's expense and final expense.

Never let taxes override a good management decision.

Agricultural Policy Topics

- Farm Bill
- WTO
- Upper Mississippi and Illinois Rivers



Energy Bill

Presented by Bob Hauser

Professor of Agricultural Economics

Farm Bill: Conservation Programs

- Conservation Security Program
  - Conference Appropriation Bill: $41 million for ’04; cap of $3.7 billion lifted for remaining 8 years
  - Many expect that the actual expenditure could be more than $8 billion
  - The “rules” of the program being held up by OMB. Still seems to be wide open for use on “working lands.”
  - Stay in touch for opportunities

Conservation Programs, Continued

- Environmental Quality Incentives Program (EQIP)
  - Approp. Bill cuts original expenditure by $25 million for ’04 to $975 million
  - The interesting issue in the future will be how much of a tradeoff takes place between EQIP and CSP

Conservation Programs, Continued

- Wetland Reserves Program: cap at 2.1 million acres
- Wildlife Preservation Program: $60 mill for ’04, increased to $85 for ’05
- Farmland Protection Program: $125 mill for ’04 and ’05, down a little after that

Mississippi & Illinois Rivers: Lock & Dam Upgrades

- Issues date back to 1978 with Inland Waterways Act, Lock and Dam 26, and user fees
- A lot of controversy over the past 25 years
- The current debate centers on the plan that the Corps will be presenting in April 2004.
  - Is a “dual” purpose plan covering navigation and ecosystem
  - Six scenarios are on the table, with the navigation upgrades ranging from $0 to $2.3 billion and the ecosystem costs ranging from $0 to $8.4 billion.

Upper Mississippi River System

- Includes Upper Mississippi & Illinois Rivers
- 35 Lock & Dams: St. Paul to St. Louis
- Outdated, deteriorating 600-foot Locks

Lock & Dam Upgrades, *cont'd*

- Easier to identify and measure costs than to identify and measure benefits
- Much of the "benefit debate" regarding navigation has hinged on what is assumed about the shape of the demand curve for barge shipments


Barge Rate
Barge Shipments

Lock & Dam Upgrades, *cont'd*

- My view: We're "missing the boat" by not paying enough attention to the location of the demand curve as opposed to it's shape.
- That is, none of the demand scenarios involving exports even come close to being "outside the box."

Lock & Dam Upgrades, *cont'd*

- Not enough attention paid to what happens under realistic futures where:
  - Major shifts among regions of the world in production, regardless total import demand
  - Major increases in export demand
  - Domestic demand for industrial use changes dramatically

Farm Bill: Payment Limitations

- 2002 Farm Bill established a Commission to study the effects of payment limits
- The Commission's August 2003 report, in general:
  - Focused on budgetary effects of recent caps as well as 25% reductions in current caps
  - Did not squarely address the issue of whether more restrictive caps should or should not be imposed.

Payment limit effects during 2000 of $40,000 on PFC payments

	Million $	% of PFC payments	% of farmers
Rice	$10.3	2.3%	4.7%
Cotton	$22.6	3.8%	2.2%
Wheat	$14.8	1.1%	0.5%
Corn	$25.7	1.1%	0.7%

General effects of tighter limits assuming no farm organization or production responses

- $40K to $30K (25% reduction) in direct payment cap leads to a 5% reduction in payments
- $65K to $50K in CC cap leads to a 5% reduction in payments at prices below loan rates
- Unlimited to $75K in loan program leads to a 4% reduction under 1999-2001 prices

Some of their other findings

- Current limits have little effect on land values nationally, nor would additional limits considered. Regional effects might be felt.
- Current "tracking" system back to individuals is poor.
- Divided on the effects of imposing an effective limit for the loan program.

Some of their recommendations

- Improve tracking of benefits to individuals through FSA
- More research
- If changes are made, don’t make them before the next Farm Bill, and then phased in.

My opinion

- If/when payments change to Illinois farmers, it will not be a result of payment limitations.

WTO negotiations

- Think of them as focusing on three locations for each country:
  - What happens at the point of production
  - What happens at the export port
  - What happens at the import port

- Point of production. Are subsidies to producers trade distorting (green, blue, amber)?
- Point of export. What are the levels of export subsidies (through price and/or credit), government-sanctioned monopolistic actions (state trading) and food aid?
- Point of import. What are the tariff levels and are there any "illegal" non-tariff trade-distortion actions?

United States

- Low distortions at import and export points, but high production subsidies.
  - Wants ROW to lower barriers at export/import ports (i.e., reduce export subsidies and import tariffs)
  - What will U.S. give up?
    - Total support payments? e.g., 5% subsidy rule
    - Specific commodities? e.g., cotton/rice versus corn/wheat
    - Specific tariffs?

Outcomes

- When?
- Effects on FTA's?
- Effects on Farm Bill?
  - This may be the most visible, direct effect on Illinois producers
  - In general, for support programs it could:
    - Discourage overall spending
    - Discourage increases in loan rates or CC prices

Country-of-Origin-Labeling (COOL)

- 2002 Farm Bill requires grocery retailers to identify beef, pork, lamb, fish, peanuts, fruits and vegetables by country of origin
- Currently in a voluntary period
- Mandatory on Sept 30, 2004 (but looks like this will be changed to 2006)
- National (USDA) mandatory i.d. system forbidden
- No 3rd party verification needed

COOL, continued

- Proponents (Some of the state livestock associations, AFB, many fruits and vegetable associations, consumer groups, …)
  - "Branding" effect: increases demand
  - Consumers want to know and this is the best way to provide this information, like any other labeling law
  - Additional records for national security, disease trace back, …

COOL, continued

- Opponents (AMI, NPPC, IFB, Administration, House Ag Chair,…):
  - Costs are high, in the form of record keeping, verification, compliance, loss of exports
    - Cost estimates have been all over the board (ISU Sparks, USDA, Florida)
    - USDA-GAO debate
  - Little evidence that demand would increase much, but this may vary by product
  - Overall, 90% is domestic

COOL, continued

- Opponents, continued
  - Guarantees labels, but not safety or traceability
  - I.D. system needed with it for efficiency and defense
  - Liability is, legally, on retailer but, effectively on producer, with additional concerns about pass-back on food safety issues
  - WTO violations and retaliation
  - Gives some countries (e.g., Canada) an advantage

COOL, continued

- Opponents, continued
  - Costs could be reduced considerably by just labeling imports
  - May encourage structural changes
  - Poultry producers win

COOL, continued

- Concluding remarks
  - House appropriation bill versus senate’s
  - Peterson’s “COOL Lite”
  - Fundamentally, this is a “branding” issue that is being treated as a “market-failure” issue

The End

Agricultural Law, Taxation & Policy: Key Issues and Developments

By Uchtmann & Endres, Hoff, and Hauser

Presented at

the "Farm Income 2004" Programs

Federal Ag Policy Issues

- Farm Bill
  - Commission's report on payment limitations
    - Effects of reducing limits on expenditures
    - Recommendations
  - Country of Origin Labeling (COOL)
    - Issues
    - Proponents and opponents
    - Studies by government and others
    - Likely outcomes

Federal Ag Policy Issues, *Cont'd*

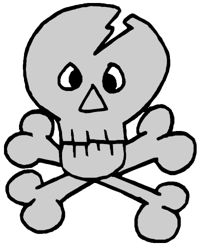
(Farm Bill, Cont'd)

- Conservation Programs
  - Appropriations for 2003
  - Appropriations for 2004?
  - Issues

- WORLD TRADE ORGANIZATION
  - Issues and stances by country/region
  - Possible outcomes
  - Effects

Federal Ag Policy Issues, *Cont'd*

- Upper Mississippi and Illinois Rivers
  - Background
  - Upgrades under consideration
  - Issues underlying benefits/costs



Energy Bill

Appendix Slides on WTO

- Provided by Bob Thompson

OECD Producer Support Estimates, 2002, in Percent

Switzerland	75
Japan	59
European Union	36
Mexico	22
Canada	20
United States	18
Australia	5
New Zealand	1

Average Producer Support in OECD Countries, 2002, in Percent

Rice	80
Sugar	48
Milk	48
Beef & Veal	37
Wheat	36
Maize	20
Oilseeds	18
Wool	6

LDCs' Own Policies Also Impede Their Development

- Corruption and/or macroeconomic instability.
- Lack of definition and/or enforcement of property rights and contracts
- Underinvestment in public goods, such as rural infrastructure and ag research
- Cheap food policies to keep urban consumers quiescent – often reinforced by food aid or subsidized exports from OECD
- Lack of technology adapted to local agro-ecological conditions (soils, climate; slope)

Uruguay Round Agreement on Agriculture: Accomplishments

- Increased market access as % of consumption
- Reduced export subsidies (value & volume)
- Converted all non-tariff barriers to tariffs
- Required scientific basis for all SPS barriers
- Acknowledged that some domestic agricultural subsidies can distort trade and categorized them by degree of trade distortion:
  - "Green box" = non trade distorting investments in public goods and decoupled income transfers
  - "Amber box" = trade-distorting (bound and reduced)
  - "Blue box" = trade-distorting, but offset by production controls or set-asides

Doha Round Must Do Better

- Uruguay Round established a useful framework
- But, it did little to open markets, and OECD countries are still spending close to US$1 billion per day subsidizing their farmers
- Doha Round can and must be more ambitious than the Uruguay Round by closing loopholes and imposing stronger controls and tighter disciplines to prevent circumvention of the intent of the agreement.

Cancun Problems

- Too many too complex issues on table
- Insufficient closure prior to arrival
- Impossibility of 148 to reach consensus
- US-EU deal seen as Blair House Redux
- G-20X overplayed its hand
- Inexperienced LDC negotiators
- EU made concessions too late
- Political constraints on US & EU going further now
- Arrogance, intransigence & brinkmanship of US and EU
- Korea & Japan’s insistence on all Singapore issues conveniently avoided addressing agriculture

Cancun Issues

- Cotton became *cause celebre*
- US-EU vs. G-20X vs. Derbez drafts
- S&D (What's a "developing" country?)
- Role of NGOs
- Special Products
- ACP concern for loss of preferences
- Singapore issues (investment, competition, customs procedures; government procurement)
- Single undertaking

Where to Now Post-Cancun

- More bilaterals and regional FTAs likely
- Election cycles dictate earliest possible conclusion = late 2005 (2007 or 2009 probably more likely)
- U.S. budget deficit will have to be addressed in 2005
- EU must broaden liberalization (while phasing out EBA exceptions)
- US and Japan have to prepare their agricultural constituencies for liberalization
- How much of the G-22 will hang together? Whither the Cairns Group? Can they cooperate?
- Expiration of Peace Clause to bring WTO cases in 2004
- Need to continue capacity building in LDCs (policy analysis, negotiating, and competitiveness)