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*Fact Sheet*

# *Direct and Counter-Cyclical Program*

**Montana State Producer Handbook**

## *Background*

The 2002 Farm Security and Rural Investment Act provided income support for wheat, feed grains, upland cotton, rice and oilseeds through two programs: Direct Payments and Counter-Cyclical Payments. The 2002 Farm Bill provided landowners a one-time opportunity to update contract base acres and farm program yields used to calculate some program benefits. Signup takes place from October 1st through June 1st of the following year.

## *Eligible Commodities*

Commodities that are covered by **direct and counter-cyclical payments** include wheat, corn, grain sorghum, including dual purpose varieties that can be harvested as grain; barley, oats, soybeans, canola, flaxseed, mustard, safflower, crambe, sesame seed, rapeseed and sunflowers including oil and non-oil varieties.
To receive payments on crops covered by the new program a producer entered into annual agreements for crop years 2002-2007. As long as producers made their initial base selection in 2003, but have not participated in the DCP program, they may do so by signing a CCC-509.

## *Producer Requirements*

- Annually, producers must sign a CCC-509 designating shares; and
- Provide actual production information for each crop year from 1998 through 2001.
- Producers with Level 2 access may use e-DCP and submit a DCP contract electronically. (CCC-509)
- Producers may also visit their local county FSA office and sign a CCC-509 to enroll.
- Producers must have a current FSA-502 (Farm Operating Plan for Payment Eligibility Review for an Individual) and an AD-1026 (Highly Erodible Land Conservation (HELC) and Wetland Conservation Certification) on file to be eligible for payments.

## *Planting Flexibility for Direct and Counter-Cyclical Payments*

- Participating producers are permitted to plant all cropland acreage on the farm to any crop, except for some limitations on planting fruits and vegetables.
- Land must be kept in agricultural uses, (which includes fallow)
- Farmers must comply with certain conservation and wetland provisions
- Annually report the use of the farm's cropland acreage
- Protect all base acres from erosion, including providing sufficient cover as determined necessary by the local FSA County Committee, and
- Control weeds.

## *Eligible Acreage (Bases)*

Farmers had a one-time opportunity to select a method for determining base acreage. Producers may update their initial acreage when their base acres have changed due to their common land unit (CLU) or CRP contracts expiring. An owner who failed to make an election was considered to have selected 2002 PFC contract acres and, for oilseed base, the minimum eligible 4-year average of oilseed plantings.

## *Payment Acreage*

Payment acreage for **direct and counter-cyclical payments** is equal to 85 percent of the eligible (base) acreage.

## *Types of Payments*

There are two types of payments:

- **Direct payments**, which are based on a fixed rate established by the Act; fixed direct payments (DP) replace production flexibility contract (PFC) payments (sometimes referred to as AMTA payments). Direct payments are not based on producers' current production choices, but are tied to acreage bases and yields.
- **Counter-cyclical payments**, which may vary depending on the crop's 12-month market price. This payment rate is

equal to the Target Price minus the Direct Payment Rate minus the higher of the loan rate or the 12-month market price.

***[(target price)-(direct payment rate)-(the higher of the loan rate or the 12-month market price payment rate)]***

Each of these payments is discussed independently in detail below.

## Direct Payments

Payment rates for wheat, corn, barley, grain sorghum, oats, upland cotton, and rice were fixed in the 2002 Farm Bill. Soybeans, other oilseeds, and peanuts were also covered under new rules established in the 2002 Farm Bill.

***Payment Yields***

Based on the current established yield for the farm, if a yield does not exist, one will be established using similar farms. Program payment yields are unchanged for those crops previously covered under the PFC program. For soybeans and other oilseeds, which were added to the program, payment yields are the farm's actual average yields for 1998-2001 multiplied by an adjustment factor (determined by dividing the national average yield for 1981-85 by national average yield for 1998-2001). The adjustment factors are as follows:

- Flax .65
- Sunflowers .80
- Soybeans .78
- All Other Oilseeds .78

If the farms actual oilseed yield cannot be determined, FSA will establish the yield using 75% of the county National Agricultural Statistics Service (NASS) average yield.

***Payment Schedule***

Issued as follows:

- For FY 2007, the advance payment rate is 22 percent and can be made beginning December 1 of the calendar year before the year when the covered commodity is harvested. Final payments are to be made in October of the year the crop is harvested.

The amount of the payment is equal to the product of the payment rate of the applicable base crop (*see page 4 of this fact sheet for direct payment rate*), the payment acres (*85 percent of base acres*), and the direct payment yields for the farm. For example, the payment for an individual wheat farmer is:

**$[(\text{Direct Payment(DP)}]_{\text{wheat}} = ([\text{Base acres}]_{\text{wheat}} \times 0.85) \times (\text{payment yield})_{\text{wheat}} \times (\text{payment rate})_{\text{wheat}}$**

***Payment Limitation Rules***

The payment limit on **direct payments** is $40,000 per person, per crop year, and the three-entity rule is retained. Under the three-entity rule, an individual can receive a full payment directly and up to a half payment from two additional entities. Producers with adjusted gross income of over $2.5 million, averaged over each of the 3 preceding tax years, are not eligible for payments unless at least 75 percent of adjusted gross income is from agriculture.

***Economic implications for Direct Payments (DP)***

Fixed direct payments are not tied to production of specific crops, the amount of production, or the price of the crop. With planting flexibility, farmers are not confined to producing crops for which they are receiving direct payments. They could receive a payment for corn, but in any given year, for example, plant wheat on the acres in which they are receiving corn payments. Thus, farmers' planting decisions are based on expected market prices and variable costs of production.
The economic impacts for DPs are similar to those for Production Flexibility Contract (PFC) payments under the 1996 Farm Bill. DPs increase farm income. Since PFC payments increased producer income and could have facilitated additional investment, PFC payments likely led to slightly higher crop production (U.S. Farm Program Benefits: Links to Planting Decisions and Agricultural Markets). However, since producers had the option of updating base payment acres in 2002 from 1996 levels, and since new crops were added to the program in 2002, farmers may have an incentive to continue producing crops and/or to expand production in order to maintain a production history in anticipation of future opportunities to expand payment acres.

## Counter-cyclical Payments

Under this program initiated in the 2002 Farm Bill, counter-cyclical payments (CCP) are available for covered commodities whenever the effective price is less than the target price.

***Payment Yields***

Three options are available to farmers to determine program payment yields for each individual crop that apply only for counter-cyclical income support payments:

- Use current program yields,
- Update yield by adding 70 percent of the difference between program yields and the farm's actual average yields for the

period 1998-2001 to program yields, or
- Update yield to 93.5 percent of 1998-2001 actual average yields.

### *Payment Schedule*

Issued as follows:

Counter-cyclical payments for the crop shall be made as soon as possible after the end of crop year for the covered commodity. For crop year 2007, there will only be one advance payment of 40 percent which will be issued after completing the first six months of the marketing year for the covered commodity. The final payment, if any, shall be made as soon as possible after the end of the crop-marketing year.
The payment amount is equal to the product of the payment rate, the payment acres (*85 percent of base acres*), and the payment yield.

For example the payment for an individual wheat farmer is:

**Payment rate $_{wheat}$ = (target price) $_{wheat}$ – (direct payment rate) $_{wheat}$ – (higher of commodity price or loan rate) $_{wheat}$**

**CCP $_{wheat}$ = ([Base acres] $_{wheat}$ x 0.85) x (payment yield) $_{wheat}$ x (payment rate) $_{wheat}$**

### *Payment Limitation Rules*

The payment limit on counter-cyclical payments is $65,000 per person, per crop year, and the three-entity rule is retained. Under the three-entity rule, an individual can receive a full payment directly and up to a half payment from each of two additional entities. Producers with adjusted gross income over $2.5 million, averaged over each of the 3 preceding tax years, are not eligible for payments unless more than 75 percent of adjusted gross income is from agriculture.

### *Economic implications for Counter-Cyclical Payments*

CCPs support and stabilize farm income when commodity prices are less than target prices. The basis for the distribution of CCP benefits may affect producers' expectations of how future benefits will be disbursed. Payments that are linked to past production may lead to expectations that benefits in the future will be linked to then past, but now current, production. Such expectations can thereby affect current production decisions. For example, farmers may not fully use planting flexibility to move from historically planted and supported crops if they expect future farm programs to permit an updating of their base acreage, which forms the foundation for payments. Instead, farmers would have incentives to build a planting history for program crops, thereby constraining their response to market prices. Similarly, use of on-land inputs that affect current yields may be influenced if farmers expect that future farm legislation will permit an updating of payment yields. In addition, since CCPs are based on current market prices, producers may view the payments as a risk-reducing income hedge. For either case, updating acreage bases or updating payment yields, economic efficiency in production is reduced because producers would not be fully responding to signals from the marketplace, but instead would be responding to market signals augmented by expected benefits of future programs and future program changes.

### *For Additional Information*

Additional information may be obtained at local FSA offices or through the Montana FSA Web site at www.fsa.usda.gov/mt/

# Deadlines/Producer Responsibilities

**October 2006 – June 1, 2007**

1. Enroll farms in DCP contracts for 2007

**February 1, 2007**

2. Begin issuing 2006 2nd Advance Counter-cyclical Payments

**July, 2007**

3. Issue 2006 Final Wheat, Barley, and Oats Counter-cyclical Payments.

**September 30, 2007**

4. 2007 DCP Late-file Signup Period Ends, $100 fee will be assessed

**October 1, 2007**

5. Begin issuing 2007 Advance Counter-cyclical Payments; Issue Final 2007 Direct Payments

**December 1, 2007**

6. Program ends with 2007

## Direct and Counter-cyclical Payment Information

**2007 Crop Year**