CRP: Green is good, but more green is preferred

Conservation Reserve Program is losing ground, but intent on enrolling more environmentally sensitive land

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Everybody wants to be green these days. A popular farmland conservation program is getting greener, yet some farmers enrolled in it are nonetheless seeing a different shade of green: the color of money.

The Conservation Reserve Program is a federal program that pays farmers and other landowners to withhold environmentally sensitive (and often marginally productive) land from production for a decade or longer. Enacted in 1985, CRP has become popular among farmers, environmental groups and policymakers for achieving the difficult dual objectives of protecting the environment while helping to stabilize farm income.

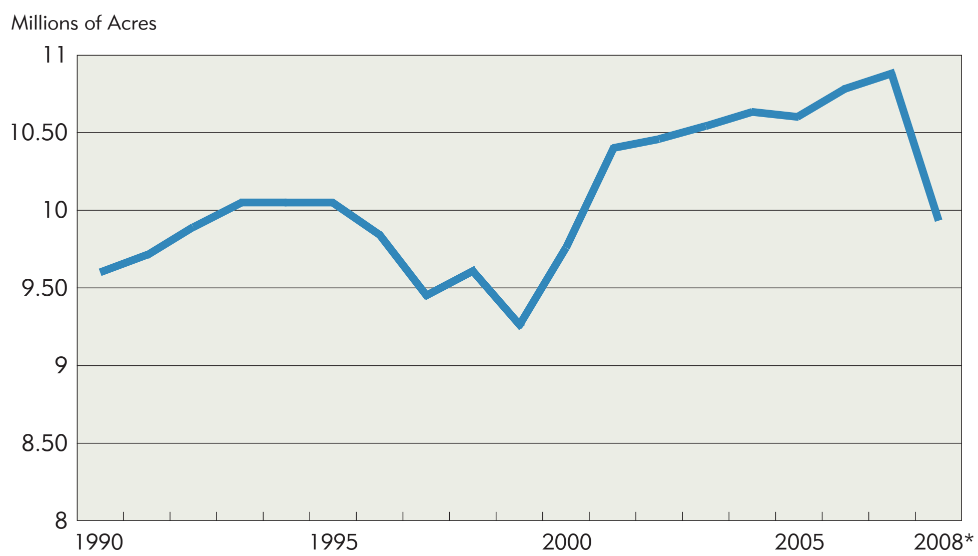
The program is undergoing a change, however. The number of acres in CRP fell significantly this past year, which grabbed headlines in district newspapers. The main reason is a booming farm economy, which has given farmers an incentive to put acres once enrolled in the program back into production.

At the same time, and largely unnoticed, the program's emphasis has been slowly shifting away from the protection of large swaths of farmland and toward strategic coverage of land with higher environmental value. The sum of these coincidental trends: Total acreage in CRP is dropping and will likely continue to fall, yet environmental outcomes might improve nonetheless.

ABCs of CRP

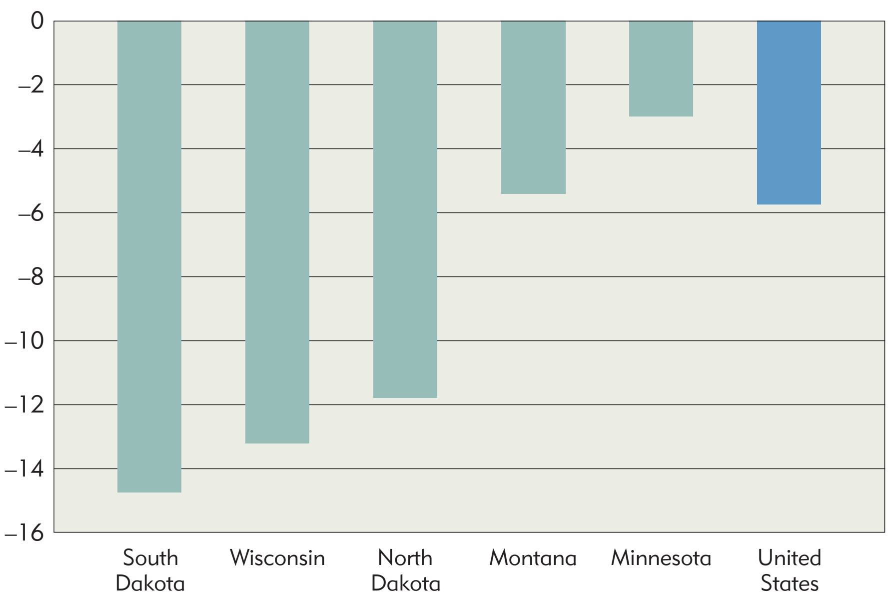
In the past year, CRP acreage declined by the largest margin ever. From September 2007 to August 2008, CRP acres nationwide declined by 2.1 million

Ninth District
Conservation Reserve Program Enrollment



*Enrollment data cover the first 11 months in FY 2008, through August. Historically, almost all enrollment changes in a fiscal year have occurred by August.
Source: Farm Service Agency, annual and monthly CRP reports

CRP Enrollment, FY 2008*



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acres, the biggest annual drop since 1998, according to data from the Farm Service Agency (FSA), the branch of the U.S. Department of Agriculture (USDA) that runs the program. (CRP contracts expire in September. At the time of this analysis, a full-year comparison—September to September—was not available. However, based on past sign-up history, almost all landowners have made their enrollment decisions in a given year by August.)

Ninth District states enroll a disproportionate number of acres in the program—about 30 percent. The decline in CRP acreage over the past year is also more pronounced in the region, dropping by about 950,000 acres, easily the highest annual decline in the district since the program's inception. CRP acreage declined in all district states, but the drop was particularly large in the Dakotas, where more than 600,000 net acres were pulled out. (See charts at left and above. Michigan was not included in this analysis because the only portion in the district, the Upper Peninsula, has a tiny share of the state's CRP acreage.)

While overall CRP acreage is declining nationally and in the district, a closer look at the program reveals two separate and divergent trends. First, a little background. Broadly speaking, CRP has two separate programs: The "general sign-up" program targets large swaths of production acreage; a second program, dubbed "continuous sign-up," protects smaller, more environmentally sensitive parcels, like those bordering waterways.

The two programs are mostly headed in different directions. The general sign-up program encompasses almost 90 percent of all CRP acres, but is shrinking. In contrast, the smaller continuous sign-up program has been growing like gangbusters, but involves a comparatively small patch of grass.

REX doesn't fetch farmers

Most of the decline in the general sign-up program has taken place in the past fiscal year and is the result of a strengthening farm sector since 2006 that has changed the economics of idling farmland. By coincidence, that same year the FSA got a sneak preview of farmer intent regarding CRP when it unveiled a sign-up program to spread out the number of contracts that expire annually.

Historically, CRP contracts have expired in large bunches at the end of each decade because there was a huge initial sign-up for the program in the latter half of the 1980s and contracts were for 10 years. In an effort to smooth expirations, the FSA introduced a re-enrollment and extension program (REX) for all general sign-up contracts expiring between 2007 and 2010, which involved about 80 percent of all CRP acres, both nationally and in the district.

The REX program did nothing to change CRP acreage at the time. Even those who planned to exit CRP still had to wait until the original contract expired. But REX opened a window to the likely enrollment trend that lay ahead for CRP, because farmers haven't been given a second chance to re-enroll in the general sign-up program after declining through REX.

After REX deadlines passed, the FSA found that only about 82 percent of general sign-up acres were renewed or extended nationwide; in the district, the renewal rate was even lower, 78 percent. The re-entry rate varied significantly among district states and was particularly low in South Dakota and Wisconsin (see chart below).

Mike Held of the South Dakota Farm Bureau said the drop in CRP acreage in that state was due mainly to landowners looking for a better return on crops. In South Dakota, corn is the number one crop, followed by wheat and soybeans, all of which are commanding high prices.

In South Dakota, for example, the

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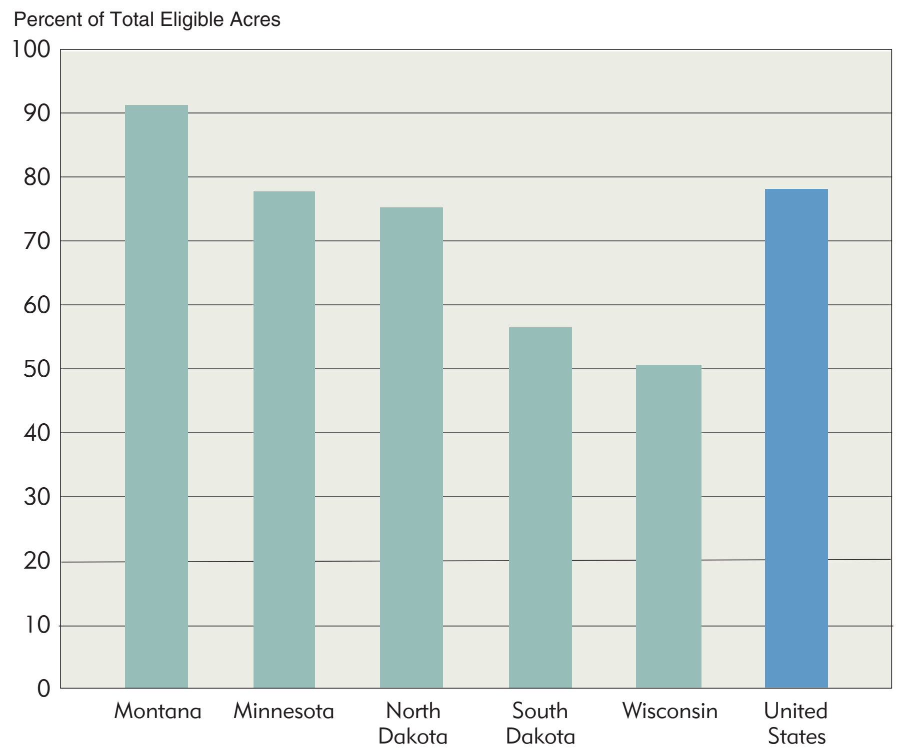
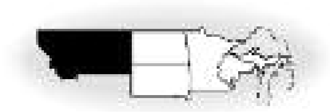
CRP Acres Re-enrolled in REX Program*



*Cumulative, 2007 to 2010 general sign-up contracts

Source: Farm Service Agency, Conservation Reserve Progam, Summary and Enrollment Statistics, 2007

MONTANA



Farmer, heal thyself

As if high fuel and feed prices weren't bad enough, farmers and ranchers in Montana are paying dearly for health care. In a 2007 survey of over 2,000 farm and ranch operators in seven states, Montana operators fared the worst from rising health care costs.

Nearly one-third of Montana operators said the cost of health care had caused financial problems, and 36 percent said they had drawn down their resources to pay for it. Those figures were higher than in the survey area as a whole.

In addition, compared with the other states surveyed (Iowa, Minnesota, Missouri, Nebraska and the Dakotas), fewer Montana farmers and ranchers had health insurance, and they paid higher premiums. In Montana, 17 percent of farming households were uninsured, compared with 10 percent on average in the other states. Montana operators who bought nongroup coverage paid a median of $11,800 annually, $600 more than the seven-state average. (Nongroup insurance costs households roughly twice as much as insurance acquired through off-farm employment.)

The survey was conducted by the Access Project, a Boston-based program aimed at improving health care in local communities, in collaboration with the University of North Dakota and Brandeis University.

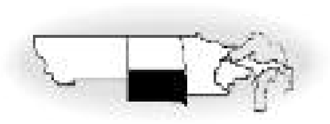
Hungry (for cash) like a wolf

A state program that compensates livestock owners for wolf kills faces a cash crunch. Since its creation last spring, the Livestock Loss Reduction and Mitigation Program has processed more than 30 claims and paid out over $17,000 to farmers and ranchers. The state anticipated that private donations would supplement $80,000 in startup funds provided by the Legislature and a conservation group. But as of September—the busy season for wolf predation—the program had not received a single donation. As a result, next year the program may be unable to cover all livestock losses.

The program will continue whether or not the state retains jurisdiction over wolves (federal wildlife officials have asked a U.S. District Court judge to restore federal protection to wolves in the Northern Rockies). One hope for permanent funding is a U.S. Senate proposal to provide federal matching funds for donations to a state livestock loss trust fund.

—Phil Davies

SOUTH DAKOTA



Down on the farm, things are way up

If South Dakota farmers have a little extra bounce this year, it's not from underinflated tractor tires.

The U.S. Department of Agriculture found that average farmland values in South Dakota grew by 21 percent in 2008, tops in the country. That's because everything farmers put in the ground is coming up roses, so to speak. Summer prices for hay and alfalfa hit all-time highs—some 30 percent over 2007 levels; South Dakota is the country's second leading alfalfa producer. This summer, more than 400 farmers pulled in $1.3 million for a carbon sequestration program run by the state's Farmers Union.

The state also expects a record corn crop of almost 570 million bushels. Better than half of that is consumed by ethanol production, which continues to expand despite low profit margins given high corn prices. This year, state ethanol producers hit 1 billion gallons from 16 plants. Four additional plants with a capacity of 260 million gallons are being explored.

Jumper cables tied to wind

Despite significant potential, the South Dakota wind industry isn't particularly well developed. But it has positioned itself to make major leaps.

During the last legislative session, the state passed a law that exempted all commercial-scale wind projects from property taxes. Instead, producers will pay a tax ($3 per kilowatt) on generating capacity as well as 2 percent on gross receipts.

This has kick-started a number of projects just since July, including a proposal for a 225-megawatt farm on Lower Brule Sioux Tribe lands and groundbreaking for a 50-megawatt farm in Brookings County. Dakota Wind Energy also publicly sought out landowners in the northeastern corner of the state for a multistage, 750-megawatt project.

But all of these will be overshadowed if a granddaddy project ever comes to fruition. Clipper Windpower had announced some time ago its interest in developing a 1,550-megawatt wind farm in South Dakota. Then this summer, the company announced it had entered a partnership with BP Alternative Energy to develop the original project and to tack on an additional and contiguous 3,500 megawatts of power in a multiphase development. If completed, it would be the world's largest wind project.

—Ronald A. Wirtz

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average payment per acre of CRP land was about $39 as of August 2008. By comparison, a South Dakota State University analysis in February calculated average returns to management and labor at more than $200 per acre of corn using a corn price of $4.24 per bushel.

Nonfarming landowners and retired farmers—folks who don't turn the soil themselves—also are finding incentives to pull land out of CRP because farmland rental rates are rising along with crop prices. In 2007, average farmland rental rates in South Dakota were 20 percent higher than the state's average CRP payment in almost two-thirds of the state's counties, according to data from the USDA. There are also widespread reports that rental rates have risen significantly in some areas this year because of high commodity prices.

(One caveat: CRP land tends to be less productive and therefore less valuable from a rental standpoint. But no data are available on rent differences between land previously enrolled in CRP and other farmland. For more discussion of trends in rental rates and other farmland issues, see the July issue of the *fedgazette* at minneapolisfed.org.)

The new CRP

A slow and relatively quiet transition also has been afoot within CRP, one that emphasizes the protection of the most environmentally sensitive land.

The continuous sign-up program is made up of smaller programs that target different types of sensitive land, particularly wetlands. Such parcels are not competitively bid (as with general sign-up, where the FSA accepts low bids to idle land) but are automatically enrolled provided the land and producer meet certain eligibility requirements.

The government pays considerably more per acre to have these sensitive tracts taken out of production. In Minnesota, payments for general sign-up acreage averaged $52 per acre last year, while payments for continuous sign-up were about $91.

The payment disparity is a big economic reason that acreage in the continuous sign-up program has ballooned since 2001, while acreage has dropped in the general sign-up program (see chart at right). However, the average parcel in the continuous program is significantly smaller—again, because it targets the most sensitive lands—which is why overall CRP acreage is down. Last year, the general program lost almost 1 million acres in the district, while the continuous program added about 26,000 acres.

Some states rich in environmental assets are seeing a more dramatic impact from increasing emphasis on the continuous program. For example, CRP acreage in Minnesota, the land of 10,000 lakes, fell the least of any district state last year—just 3 percent. In 2008, 22 percent of the state's CRP acreage was enrolled in the continuous program, compared with the national average of 12 percent.

The trend line for both CRP programs appears unlikely to slow down or veer anytime soon. For example, the FSA extended this year's annual deadline to transfer general sign-up land into the continuous program from September to May, giving landowners an extra eight months to choose that option after their original contracts had expired.

For the general sign-up program, high commodity prices have ratcheted up pressure to farm all available land, and the program is not actively seeking new general sign-ups. For the past two years, USDA Secretary Mike Johanns announced there would be no new sign-ups for the general program, and a Wisconsin FSA representative said there will be no general sign-ups offered in the next few years.

This news goes hand-in-hand with the latest provisions outlined in the 2008 farm bill passed last May that capped CRP acreage at 32 million acres nationwide, a 7 million acre reduction from the 2002 farm bill. August enrollment stood at 34.7 million acres. The new cap must be achieved by 2010 and will remain in place until 2012.

Looking for cover

Despite pressures driving down overall CRP acreage, a stampede out the door is unlikely. First, opting out of CRP contracts early carries stiff penalties: All CRP payments over the lifetime of the contract must be repaid, along with a penalty fee.

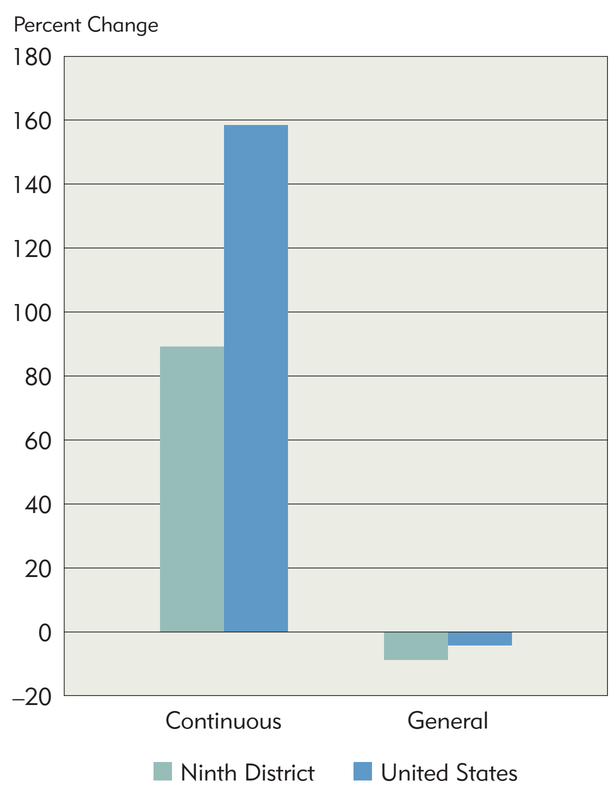
Getting out of a contract is even more problematic for most landowners who, back in 2006, participated in REX. Through the program, roughly three-quarters of contracts—many of which would now be expired or nearing expiration—were extended for two to five years. Sounds innocuous enough, but lengthening the contract increased the cost of opting out. The most environmentally prized land received new contracts in the REX program, which reset the repayment ticker for contract holders who decide to terminate early.

Current farm conditions have put added pressure on the FSA to allow CRP contract holders to opt out early without penalty; with considerable acreage tied up in CRP, the farm sector hasn't been able to respond to rising global demand for a variety of commodities, but especially for corn, which is being driven by increasing ethanol production. Many states that before were not known as ethanol producers are experiencing a boom.

"Six or seven years ago, Wisconsin did not have any ethanol plants," said Paul Zimmerman, from the Wisconsin Farm Bureau. "Today, we have seven plants in our state."

Despite considerable lobbying earlier this year for the USDA to waive early opt-out penalties for CRP contracts, Johanns indicated that the agency would not oblige. Environmentalists and sportsmen's groups oppose early opt-outs. Many bird hunters, for example, believe that CRP has been critical to

Enrolled Acres, 2001 to 2008
Continuous vs. General Sign-up Programs



Source: Farm Service Agency, annual and monthly reports

CRP land in the Prairie Pothole Region of the Dakotas has contributed to measurable gains in wildlife populations.

improved hunting conditions. In the Prairie Pothole Region of the Dakotas, CRP land has contributed to measurable gains in wildlife populations. An FSA-commissioned study last year of grassland bird populations in the region credited CRP with increases of roughly 1.1 million bobolinks and 320,000 sedge wrens.

Agricultural considerations also play a role in CRP enrollment in district states. Montana, for example, saw only a 5 percent drop in CRP acreage this year. Despite good moisture this year, Montana is not far removed from drought conditions, which makes it economically difficult for farmers to take their land out of the program, according to Glen Patrick from the Montana FSA office. He pointed out that it takes a great deal of inputs to get land back into production in the first year when the ground is dry. (An analysis this past summer by Dwight Aakre of the North Dakota State University Extension Service calculated the startup costs of bringing CRP back into production in that state at almost $55 an acre.)

The type of crops grown in a state also has a bearing on how much CRP acreage gets plowed up. Though crop prices have been high virtually across the board, corn and soybeans tend to offer better returns, particularly in certain areas. That's probably another reason CRP exits have been lower in Montana, according to John Youngberg of the Montana Farm Bureau, because neither corn nor soybeans are a major crop in the state.

"In areas where they plant higher-value crops such as corn and (soy)beans, it may be more economically feasible to plow up CRP. In Montana, where the majority of our cropland is wheat or barley, it might not be as compelling an argument," Youngberg said.

Looking for more green

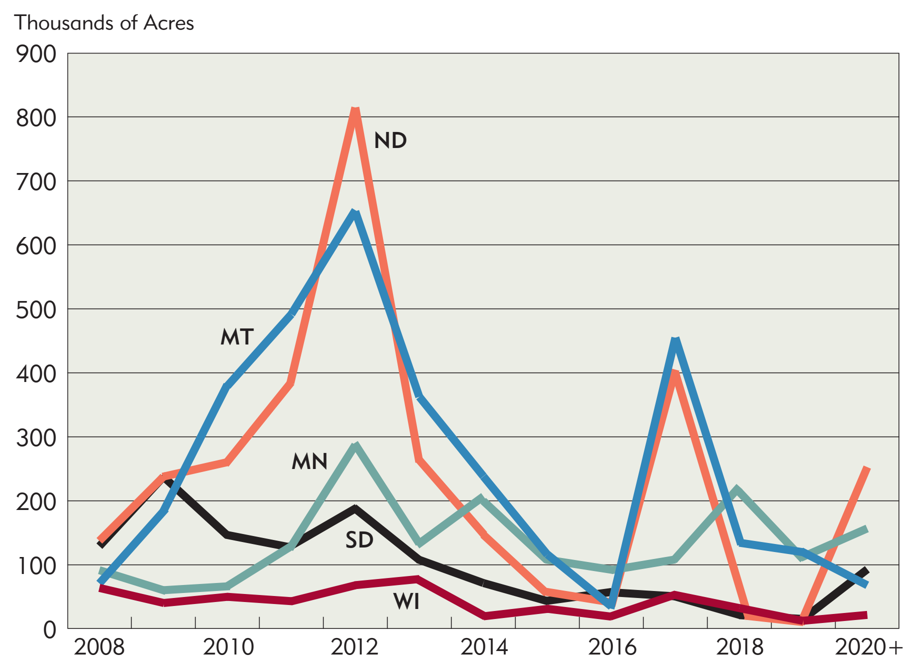
There has been much speculation about the future of CRP in light of strong farm commodity prices.

Thanks to the many thousands of CRP contracts that saw short-term extensions under REX, better than half of all contracts will expire between 2009 and 2012. From now through 2020, each district state will see a varying trend of expiring acreage, but a clear and growing spike awaits in 2012 (see chart below). The question is how much of that acreage will be re-enrolled.

In the long run, farm prices will dictate the level of participation in the general sign-up program. Should prices stay high, enrollments are likely to decline unless the program raises average payments.

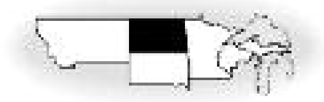
At the same time, however, states are starting new programs that coincide with federal interests in targeting more environmentally valuable land for retirement. Earlier this year, for example, the South Dakota Department of Game, Fish and Parks proposed enrolling 100,000 acres in the James River Watershed Basin—widely recognized for its great potential as a wildlife habitat—into a specific CRP environmental program. This would be the first program of its kind in the state, and supporters hope that it will improve water quality and help reduce soil erosion as well. f

CRP Acreage by Year of Contract Expiration



Source: Farm Service Agency; data as of January 2008

NORTH DAKOTA



Burying the new jar of money

North Dakota is adding another crop to its list of harvests: carbon.

The North Dakota Farmers Union is already a sophisticated player in the market for so-called carbon credits, coordinating contracts for about 2,300 farmers nationwide and selling the credits on the Chicago Climate Exchange (see the July 2008 *fedgazette* online at minneapolisfed.org). More than 40 percent are North Dakota farmers, who pulled in about $2.6 million this year, according to the organization. Now state landowners are being offered another carbon venue: In August, Ducks Unlimited unveiled a new program spearheaded through the Department of Energy and the U.S. Fish and Wildlife Service to offer cash payments to those with land in the Prairie Pothole Region. The program will offer payment for a perpetual easement on the land, as well as a second, smaller payment for the carbon sequestration. Combined, the two would add up to about $36 per acre, according to local reports.

For some, the perpetual easement may be a roadblock; the Farmers Union and other sequestration programs often offer five- and six-year contracts.

Whistling past the graveyard

If North Dakotans seem quiet when it comes to the economy, they're probably just trying to keep from bragging.

While much of the country struggles, North Dakota has boomed. In 2007, taxable sales jumped by 10 percent, topping $10 billion for the first time. In the first quarter of this year, taxable sales accelerated to 13 percent. That same quarter, personal income skyrocketed by 7.6 percent—more than double the rate in the next closest state (South Dakota). Nationally, quarterly personal income grew by 1 percent.

A gushing oil industry has been a major driver—evident in part by the fact that the state's four largest cities saw lower growth in 2007 taxable sales compared with the statewide average. But other sectors are contributing to overall growth. State reports show that 14 of 15 industries in the state saw growth last year, and that momentum is spilling over. In the first quarter of this year, mining and oil extraction taxable sales were up an amazing 60 percent, but manufacturing also registered almost 20 percent growth, and wholesale trade jumped almost 30 percent.

—Ronald A. Wirtz