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Reviewing the USDA Proposal to Limit Farm Program Payment Eligibility

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On March 24, 2015, USDA announced a proposed rule that further restricts farm program payments to those persons who are actively engaged in farming. USDA's proposed rule is the result of the 2014 Farm Bill; it seeks to limit the number of individuals who previously qualified for farm program payments based solely on providing management to the farm operation rather than labor. This article reviews the proposed regulation in light of the public comment period which allows anyone to submit comments on the proposed rule by May 26, 2015. (Note: a version of this article is also available at Policy Matters, a companion website providing analysis on a wide range of topics).

Background

Requiring a person be actively engaged in farming to receive federal farm payments was a reform introduced by the House Agricultural Committee as part of the Omnibus Budget Reconciliation Act of 1987 (P.L. 100-203, passed December 22, 1987). It was intended to address "methods to legally circumvent" payment limitations and "schemes [that] have been developed that allow passive investors to qualify for benefits intended for legitimate farming operations." (H. Rept. 100-391 (Oct. 26, 1987), pg. 14-16); H.R. 3545). A General Accounting Office report at the time had highlighted the issue and Congress responded by prohibiting payments to anyone not considered actively engaged in farming.

Under the current statute and regulation, a person can qualify for farm program payments if they are actively engaged in farming, which means they have made a significant contribution of both: (1) capital, equipment, or land; and (2) personal labor or active personal management. The controversy debated for this farm bill is similar to the one raised in 1987: passive investors are able to collect payments intended for farmers by claiming to provide management to the farm (in addition to capital, equipment, or land). Farms that are organized as general partnerships or joint ventures are permitted to increase total payments to the farm entity for each additional person added to the operation. This has led to concerns about whether the management requirement was failing to properly limit program payments.

The issue was part of the 2014 Farm Bill debate. Both the 2012 and 2013 Senate versions of the farm bill sought to strike the phrase "active personal management" and limit additional payments to only a single farm manager in an operation. The same provision was added during debate on the House floor as part of an amendment that passed by a vote of 230 to 194. As reported at the time, this was among the final and most difficult issues to resolve in the conference negotiations between the House and Senate (see here, here, here and here). The final conference compromise directed USDA to address the issue. First, USDA was required to write regulations to define the term "significant contribution of active personal management" for the actively engaged in farming eligibility requirement. Second, USDA was given the authority to limit the number of persons qualifying for payments as a farm manager. USDA was not, however, permitted to apply the regulation to farms consisting entirely of family members. USDA has published the proposed regulation in response.

Before undertaking further discussion (and in the interests of full disclosure), I want to acknowledge my involvement with this issue. I served on the Senate Agriculture Committee staff for then-Chairwoman U.S. Senator Debbie Stabenow during the 2014 Farm Bill debate. I also served as Administrator of the Farm Service during implementation of the 2008 Farm Bill. The issue arose during that process as well, however, no proposed or final regulation on it was published.

Discussion

Towards the end of the farm bill debate, the U.S. Government Accountability Office (GAO) produced a report which highlighted concerns with the current statute and regulation, concluding that revisions were needed to the actively engaged in farming eligibility requirement. This report provides context to the farm bill debate and USDA's proposed changes. GAO focused on how general partnerships use managers to collect additional farm program payments. For example, GAO found that general partnerships constituted roughly 27 percent of all entities receiving payments in 2012 but collected over 49 percent of the total payments. Moreover, GAO found that general partnerships received 97 percent of their total farm program payments through managers, either alone (27 percent) or in combination with labor (70 percent). By comparison, general partnerships received only 3 percent of their total farm payments due to persons contributing only labor to the farm. In other words, these entities are getting the bulk of their farm program payments by adding managers to the farm. GAO also provided specific examples to demonstrate usage of the rule (see page 35 of the report) as did Senator Grassley in a 2014 Farm Bill implementation hearing on May 7, 2014 (available here, beginning at 1 hour 30 minutes). The top three are summarized here:

- A farm in Louisiana had 22 members (all of them Limited Liability Companies) with 16 of the members qualifying for payments as managers. The farm operation received $651,910 in federal payments in 2012.

- A farm in Arkansas had 26 members (all corporations) with 6 members qualifying for payments as managers only and 15 qualifying through a combination of management and labor. The farm received $582,876 in federal payments in 2012.

- A farm in Mississippi had 11 members, 6 of them qualifying for payments as managers. The farm received $440,000 in federal payments in 2012.

The proposed rule would add eligibility requirements for farms seeking to qualify multiple managers for farm program payments. The new requirements would not apply to farm operations that consist entirely of family members. Existing provisions for landowners who share in the risk of a crop and for spouses are also not altered by the proposed rule. If the farm operation contains any non-family members then it can only have one person qualify for farm program payments as a manager under the existing rules. Any additional person seeking to qualify for payments as a manager must meet the new requirements.

The proposed regulation defines "active personal management" to mean those items critical to the profitability of the farming operation. It divides management activities into categories of farm capital, labor, agronomics and marketing. Only significant contributions count, meaning a person must perform such activities on a "regular, continuous and substantial basis" consisting of either 25 percent of the total management hours required by the farm operation or at least 500 hours annually. These requirements, however, appear not to apply to the first farm manager in the operation.

No farming operation may qualify more than three persons for payments as managers and an operation can have one manager qualify under existing requirements. If the farming operation seeks to qualify more than one person as a manager, then each such person is required to keep records or logs of their activities. Qualifying additional managers is not automatic. A farm must be considered large (producing crops from more than 2,500 acres, honey from 10,000 hives or wool from 3,500 ewes) to qualify one additional person for payments as a manager. A farm claiming to be complex may seek to qualify one additional person for payments as a manager. Complexity will be determined by the number and type of livestock, crops or other agricultural products and the geographical area covered. FSA state committees must agree that a farm is complex. State committees are also given authority to adjust the requirements by 15 percent if they determined that the relative size of farming operations in the state requires it. If a farm operation seeks to qualify the maximum three persons for payments as managers, it must be both large and complex.

The proposed regulation only applies to general partnerships and joint ventures because only those entities can increase payments by adding people. For example, a general partnership with two partners can receive a total of $250,000 ($125,000 per partner). If the general partnership adds another partner who is considered actively engaged the total limit for the entity increases to $375,000. The proposed regulation is not expected to impact corporate or LLC entities because they cannot increase payments in this fashion. Corporations and Limited Liability Corporations (LLCs) are subject to a single payment limit per entity ($125,000 under the 2014 Farm Bill) without regard to the number of shareholders or members in the farming entity. This distinction is based on the statute which provides an exception for general partnerships and joint entities from the general limit; payments to these entities may not exceed the payment limit multiplied by the number of persons and legal entities constituting the general partnership or joint venture. (7 U.S.C. §1308(e)(3)(B)).

By limiting the use of farm managers to multiply payments, the proposed changes appear to address many of the concerns with the current rules. A few notable issues remain and are briefly discussed here for the reader's consideration. As an initial matter, the differential treatment of entity types when it comes to payments is not addressed here because it is provided for in the statute and may need Congressional action to change it.

The proposed changes create differential treatment for farm managers without much explanation or justification. USDA could provide more clarity on how the changes apply to the first farm manager. USDA may also want to explain or justify exempting the first farm manager from the new definitions applied only to the additional managers. A similar issue arises with the recordkeeping requirement. Again, the proposed rule provides different treatment for the first farm manager than for additional managers. In addition to reconsidering treating all farm managers the same, USDA might also want to consider whether this recordkeeping should also come with a reporting requirement. The long-standing concerns about this issue would seem to counsel verification of compliance with the regulation.

Additionally, among the categories of active personal management activities, USDA has included participation in USDA programs. Because a person need provide only one of the categories of activities to qualify, it appears possible that filling out USDA program paperwork could qualify a person for payments as a manager. The final regulation may want to clarify this and USDA may want to reconsider whether this activity is substantive and appropriate to qualify an individual for a farm program payment.

Conclusion

The proposed rule is part of a long debate about the validity of allowing farms to use passive investors or managers to collect additional farm program payments. Whether more or less should be done remains open for debate. Opposition to the proposed rule can be expected to push for significant changes in the final rule. Historically, they have argued that because some farms are large and complex they require multiple managers. It is worth noting that nothing in the proposed rule limits the number of managers a farm may have; it limits only the amount of additional program payments the farm can receive. Farm size and complexity seem to be of questionable relevance here and provide little justification for allowing some operations to multiply payments. Supporters of the principles behind this rule might question whether it has gone far enough. They may seek further limitations on the ability to receive additional payments but could find USDA's authority limited by statute as well as politics. They may find that USDA has more room to maneuver around specific issues such as equitable treatment for all farm managers and reporting requirements. The final rule is yet to be determined and everyone has until **May 26, 2015**, to submit comments on the proposal to USDA. They can be submitted online at http://www.regulations.gov or at the mailing address provided in the rule.

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