

# RECENT DEVELOPMENT

## RISING CROP PRICES AND THE EFFECT ON THE CONSERVATION RESERVE PROGRAM

As fuel prices have steadily increased and fears of energy security have become more serious, demand for alternative fuel sources has grown.<sup>1</sup> While alternative fuel sources may provide some benefits, they also have the potential to create a wide array of new problems.<sup>2</sup> The most prevalent alternative fuel in the United States is ethanol, which is made predominantly from corn.<sup>3</sup> Demand for ethanol is rising and has thus created a growing demand for corn.<sup>4</sup>

The effects of this increased demand are complex and have been analyzed in many different ways. Price increases per bushel of corn are the most apparent effect.<sup>5</sup> The price of corn has historically remained stable at approximately two dollars per bushel but has recently doubled to approximately four dollars per bushel.<sup>6</sup> The increased price has affected many different aspects of the economy. First, the price of corn has a large impact on the livestock industry because of its use as a feed source.<sup>7</sup> If the price of corn becomes too high, the likely effect will be a decrease in livestock supply and an increase in the price of meat. The second effect is that as corn prices rise, farmers, to satisfy the large demand, will devote more of their land to corn.<sup>8</sup>

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1. Michael S. Rosenwald, *The Rising Tide of Corn, Ethanol-Driven Demand Felt Across the Market*, WASH. POST, June 15, 2007, at D01, available at [http://www.washingtonpost.com/wpdyn/content/article/2007/06/14/AR2007061402008\\_pf.html](http://www.washingtonpost.com/wpdyn/content/article/2007/06/14/AR2007061402008_pf.html).

2. Lori Weaver, *Controversy Continues Over Ethanol's Impact on Feed and Food*, FEED MANAGEMENT, July/August 2007, at 8-9.

3. Rosenwald, *supra* note 1.

4. *Id.*

5. Weaver, *supra* note 2, at 8.

6. Rosenwald, *supra* note 1.

7. *See* Weaver, *supra* note 2, at 8.

8. *Id.*

Conversely, less land will be devoted to growing other crops such as soybeans and wheat, causing other supply shortages and price increases. Therefore, it is easy to see why many people are concerned about the prospect of an ever-increasing demand for ethanol and corn.<sup>9</sup>

Increasing the amount of farmable land in the United States is one possible remedy to this situation.<sup>10</sup> Currently, millions of acres of potential farmland are not being farmed because of their enrollment in the Conservation Reserve Program (“CRP”).<sup>11</sup> This program is a federally funded lease program where the United States Department of Agriculture’s (“USDA”) Farm Service Agency (“FSA”) pays landowners not to farm their land.<sup>12</sup> The CRP began in 1985 as a means to control the supply of wheat and feed grains in the market and thus help farmers control prices.<sup>13</sup> But in 1990 the objectives of the program were altered to consider the environmental benefits of conserving certain land areas and avoiding abusive farming practices.<sup>14</sup> The land enrolled in CRP is generally subject to a ten to fifteen year contract whereby the landowner receives rental payments and must pay a significant penalty to remove the land and begin farming it early.<sup>15</sup> Rental rates paid by the FSA to the landowner are based upon the inherent productivity of the soil along with an accounting for the level of environmental benefit.<sup>16</sup>

The CRP has provided many environmental benefits over its more than twenty-year existence. One positive benefit is the reduction of soil erosion.<sup>17</sup> According to the FSA, CRP has reduced soil erosion rates by an estimated 450 million tons per year and protected 25 million acres of highly erodible cropland

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9. *Id.*

10. Art Hovey, *Rising Crop Prices Pose Threat to Conservation Program*, LINCOLN JOURNAL STAR, Jan. 10, 2008, available at <http://journalstar.com/articles/2008/01/10/news/local/doc47855faf648f4601510768.txt>.

11. James B. Johnson & Richard T. Clark, *THE CONSERVATION RESERVE PROGRAM* (2003), available at <http://www.farmfoundation.org/news/articlefiles/35-jbjohnson.pdf>.

12. Rachael Neile-McGrew, *US Farmers Putting More Soil Under the Plow*, CELSIAS, Jan. 26, 2008, <http://www.celsias.com/2008/01/26/us-farmers-putting-more-soil-under-the-plow/>.

13. Silvia Secchi & Bruce A. Babcock, *Impact of High Crop Prices on Environmental Quality: A Case of Iowa and the Conservation Program 1* (Center for Agricultural and Rural Development, Iowa State University, Working Paper 07-WP 447, 2007), available at [http://www.econ.iastate.edu/research/webpapers/paper\\_12804.pdf](http://www.econ.iastate.edu/research/webpapers/paper_12804.pdf).

14. *Id.*; Neile-McGrew, *supra* note 12.

15. Secchi & Babcock, *supra* note 13, at 1.

16. Johnson & Clark, *supra* note 11, at 2.

17. FARM SERV. AGENCY, U.S. DEP'T OF AGRIC., *CONSERVATION RESERVE PROGRAM: SUMMARY AND ENROLLMENT STATISTICS FY 2006* (2007), available at <http://www.fsa.usda.gov/FSA/webapp?area=home&subject=copr&topic=crp-st>.

from erosion.<sup>18</sup> Another benefit realized from this program is enhanced water quality. CRP has protected surface and ground water from sediment and nutrient enrichment by enrolling millions of acres of streamside grass and forested buffers, along with specifically enrolling certain wetland restoration areas.<sup>19</sup> The program has also created many benefits for wildlife populations through increased habitat.<sup>20</sup> There have been many studies showing the benefits that game birds, such as the pheasant and bobwhite quail, have experienced because of CRP.<sup>21</sup> The Secretary of the USDA, Mike Johanns, asserted that CRP “provides more habitat for birds and other species than all of the national wildlife refuges combined.”<sup>22</sup> Yet another benefit, which has become an important issue recently, is the carbon sequestration effects of CRP.<sup>23</sup> The FSA estimates that fifty million metric tons of carbon dioxide are sequestered in soils and vegetation annually on enrolled lands.<sup>24</sup>

There are several ways that landowners may remove lands from CRP to start planting crops such as corn. The first method is to wait until the expiration of their CRP contract and refuse to renew it.<sup>25</sup> There are a large number of contracts expiring in the next few years and many fear that landowners will be influenced by high corn prices to decline to renew their CRP contracts.<sup>26</sup> The USDA estimates that farmers with expiring contracts will withdraw 4.6 million acres (of the total thirty-six million acres of enrolled land) from the program in the three years following 2006.<sup>27</sup> The other way landowners may remove land from the program is by terminating their contract and paying a penalty.<sup>28</sup> Historically, this financial penalty has been set high enough to deter most landowners from exiting the program before their contract runs out, but, as crop prices increase, it may become

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18. *Id.* at 5.

19. *Id.*

20. *Id.* at 5-6.; *see also* Patrick Sullivan et al., *Land-Use and Economic Implications of Expiring CRP Contracts*, THE CONSERVATION RESERVE PROGRAM: ECONOMIC IMPLICATIONS FOR RURAL AMERICA at 45, AGRIC. ECON. REPORT NO. (AER-834) (2004), available at <http://www.ers.usda.gov/Publications/aer834/> (follow “Land-Use and Economic Implications of Expiring CRP Contracts”).

21. FARM SERV. AGENCY, *supra* note 17, at 5.

22. S. Regional Extension Forestry, Land Enrolled in CRP Should Stay Put, USDA Secretary Says (2007), [http://www.soforext.net/news\\_items/News\\_Item.2007-04-06.1225](http://www.soforext.net/news_items/News_Item.2007-04-06.1225).

23. Secchi & Babcock, *supra* note 13, at 1; FARM SERV. AGENCY, *supra* note 17, at 6.

24. FARM SERV. AGENCY, *supra* note 17, at 6.

25. *Id.* at 4.

26. S. Regional Extension Forestry, *supra* note 22.

27. *Id.*; Johnson & Clark, *supra* note 11.

28. Annie Baxter, *Corn Crunch Puts the Squeeze on Conservation Program*, MINN. PUB. RADIO, May 2, 2007, <http://minnesota.publicradio.org/display/web/2007/04/17/crp/>.

efficient for them to terminate their contracts.<sup>29</sup> Before making such a decision, the landowner must estimate potential profits and consider the costs of converting the CRP land to farmland and of actually farming the land.<sup>30</sup> Therefore, landowners need to consider factors other than crop prices when making their CRP contract decisions. The cost of petroleum-based fuel will be a major consideration in determining potential farming profits. Ironically, the industry that is trying to provide alternative fuel sources must use large amounts of petroleum-based fuel, usually diesel, in order to produce ethanol.<sup>31</sup> So if land is taken out of CRP and the amount of farmed land increases, the increase in demand for an alternative fuel source will have effectively created more of a demand for petroleum-based fuel. Therefore, the intended environmental benefit of increasing the use of ethanol may be offset by the large amounts of petroleum-based fuel needed to produce it.

Most landowners will act rationally and make decisions to maximize the profit from their land. Therefore, as farming and farmland rentals become more profitable, CRP payments and penalties must also increase in order to keep the land enrolled in the program. If the program rental payments do not exceed the expected profits from farming the land then it is expected that most farmers will not hesitate to let their contracts expire. Landowners should not be expected to consider all of the potential environmental benefits that the enrolled land is providing. Although some environmental benefits directly benefit the landowners, there are many more indirect benefits that most landowners will not feel responsible for maintaining and will not consider when deciding whether to renew their CRP contract. It may be argued that the government should be the responsible party for ensuring environmental quality that would otherwise be overlooked if left up to individuals. Thus, it may be concluded that the government should increase their spending in CRP and simply increase their rental prices to coincide with the rising crop prices.

However, others argue that most of the land controlled by CRP is not very good farmland and making it profitable would be very difficult for farmers.<sup>32</sup> Therefore, there would be no need for an increase in CRP rental rates because while the land that is

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29. *Id.*

30. Sullivan et al., *supra* note 20, at 45-46.

31. Gary Wulf, *Oil Costs Fuel Crop-Market Changes --- U.S. Growers are Planting More Efficient Commodities, Such as Soybeans, Over Corn*, THE WALL STREET JOURNAL, May 8, 2006, at C4.

32. Baxter, *supra* note 28.

now profitable is becoming more profitable, the inferior land enrolled in CRP is still not capable of being converted from no profits to high profits. It also follows that this inferior farmland would not have a large impact on corn prices because it would not produce a large enough amount of corn to affect the overall market.<sup>33</sup>

One study by John Urbanchuk evaluates the problem of increasing food prices, arguing that increased energy prices have a much larger impact on the price of food than increased corn prices.<sup>34</sup> Urbanchuk recognizes that the Consumer Price Index (“CPI”) for food has been increasing at a very rapid rate recently, but that the potential benefits of decreasing fuel prices through ethanol production would have a positive impact on food prices that would outweigh those imposed by increased corn prices.<sup>35</sup> Urbanchuk’s data suggests that an increase in petroleum prices will have close to twice the impact on consumer food prices as equivalent increases in corn prices. The data shows that a thirty-three percent increase in crude oil prices would increase food prices by 0.6 to 0.9 percent, while an equivalent price increase in corn (about one dollar per bushel) would increase consumer food prices only 0.3 percent.<sup>36</sup> Urbanchuk further asserts that the increase in food prices have been more a product of foods independent of corn, such as fish, fruits, and vegetables, as opposed to corn dependent foods such as meat, poultry, eggs, and dairy. His data shows that these corn dependent foods only “accounted for 0.2 percent of the 1.2 percent acceleration in food price inflation between 2006 and April 2007.”<sup>37</sup> Urbanchuk concludes that the reason petroleum and energy prices have such a significant impact on food prices is that energy affects all aspects of food production. Energy prices affect the production, packaging, and distribution of all agricultural products, whereas corn only affects one segment of consumer food products.<sup>38</sup>

The interaction of fuel alternatives and effects on the crop market are complex. The possible economic incentives to shift farmland from environmental benefits to crop production is also not completely understood. Ethanol production has certainly affected the price of corn, but whether ethanol’s overall impact on

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33. *Id.*

34. John M. Urbanchuk, Director, LECG LLC, “*The Relative Impact of Corn and Energy Prices in the Grocery Aisle*,” 7-8 (2007), available at [http://www.ethanolrfa.org/objects/documents/1157/food\\_price\\_analysis\\_-\\_urbanchuk.pdf](http://www.ethanolrfa.org/objects/documents/1157/food_price_analysis_-_urbanchuk.pdf).

35. *Id.* at 7.

36. *Id.* at 1.

37. *Id.* at 2.

38. *Id.* at 5.

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the economy and the environment will be positive remains to be seen. The USDA and the FSA have a very difficult and complex decision to make concerning the direction of the CRP. They must weigh the environmental benefits of the program against the potential benefits of allowing a large number of land tracts to be removed from the program. The decision to be made is whether they will raise the CRP land rental payments to keep up with rising crop prices and whether they believe crop prices will continue to rise. This is yet another issue that has been created by the larger need for an alternative fuel source in the United States. As policy changes occur, there will inevitably be unintended side effects, and we can only hope that decision-makers will consider all possibilities and make decisions that create the most overall favorable result.

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