Marketing Assistance Loans, Loan Deficiency Payments and Marketing Loan Gains for Minor Oilseed and Pulse Crops

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Objective Analysis

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Decision Making

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Marketing assistance loans are available to Montana producers of minor oilseed and pulse crops. The USDA differentiates county-level loan rates from national rates for minor oilseeds and dry peas . County-level lentil and small chickpea loan rates for all pertinent counties throughout the United States are differentiated at the multi-state, regional level from the national loan rates. Montana county-level rates for the 2003 crop year are shown in Appendix A: Figures 1 through 7 for canola, crambe, flaxseed, mustard, rapeseed, safflower, and sunflower. For each of the pulse crops-- dry peas, lentils, and small chickpeas the county-level loan rates are the same in all Montana counties, as reported in Table 1.

Loan deficiency payments are available on all or a portion of harvested production when posted-county prices for a loan commodity are below county-level loan rates. Similarly, marketing loan gains are available when posted-county prices are less than county loan rates at the time marketing assistance loans are settled.

Mechanisms for determining loan deficiency payments and marketing loan gains are described. Mechanisms for determining posted-county prices are described including the use of differentials for each commodity. Differentials specified by the USDA, generally considered some depiction of commodity transportation and elevation costs, are shown for the 2003 crop year for all Montana counties in Appendix B, Figures 8 through 14 for canola, crambe, flaxseed, mustard, rapeseed, safflower, and sunflower.

Introduction

Prices for many storable agricultural commodities are often relatively low at harvest when compared to other times throughout a marketing year. Some producers store loan-eligible commodities on their farms at harvest. In some cases these commodities are already priced and delivery will occur as scheduled by the producer and buyer. Other producers may obtain a marketing assistance loan from the Commodity Credit Corporation (CCC) at or soon after harvest in anticipation of a price premium for storing their commodity. Subsequently they can settle their marketing assistance loan and sell their stored production. Or in periods of relatively low prices at or soon after harvest producers may choose to receive a *loan deficiency payment* for not placing all or a portion of their loan-eligible production under a marketing assistance loan.

Producers who place their production under loan may recapture their production held as loan collateral prior to loan maturity. They can realize a *marketing loan gain* when they are able to repay their loan at a *posted-county price* that is less than the loan rate (price) at which the loan was taken.

Marketing assistance loans essentially establish a price floor for production of loan quality. Marketing assistance loans are used by some producers as a source of cash to meet short term cash flow needs until they deliver production that was stored at harvest.

Marketing Assistance Loans

Marketing assistance loans for minor oilseed commodities have existed under Federal legislation since the 1991 crop year. In 1990, under authority of the Food, Agriculture, Conservation and Trade Act (FACT Act), the marketing assistance loan program was extended to minor oilseed crops. Subsequent Federal commodity legislation has maintained the marketing assistance loan program for minor oilseed crops.

County-level loan rates for each minor oilseed crop usually differ from their respective national loan rates. The Farm Service Agency (FSA) of the United States Department of Agriculture (USDA) differentiates county-level loan rates from national rates. FSA uses factors such as location of a county relative to terminal markets when establishing the county-level loan rate for a commodity.

County-level marketing assistance loan rates for minor oilseed crops for the 2003 crop year, expressed on a per hundredweight basis, are shown in Appendix A, Figures 1 through 7.

Marketing assistance loans for select pulse crops were authorized under the Farm Security and Rural Investment Act of 2002. Loans are available for lentils, dry peas, and small chickpeas.

County-level loan rates for dry peas are differentiated from national loan rates considering factors such as location of the county relative to the pertinent terminal market when setting county-level loan rates.

For the 2003 crop, the dry pea loan rate for all counties in Montana is $0.44 per hundredweight less than the national-level loan rate per hundredweight (Table1). The loan rate for dry peas for all counties in North Dakota and all other states in the “eastern” region are the

same as those in all Montana counties. The eastern region includes all states except those in the "western" region that includes Arizona, California, Idaho, Nevada, New Mexico, Oregon, Utah, and Washington.

For the 2003 crop year all counties in Montana have the same lentil loan rate per hundredweight and the same small chickpea loan rate per hundredweight. These loan rates prevail in all counties in the United States and are the same as the national loan rates.

Table 1: Pulse Crop Loan Rates per Hundredweight for the 2003 Crop Year

Crop	National Rate	All Montana Counties
Dry peas	$ 6.33	$ 5.89
Lentils	$11.94	$11.94
Small chickpeas	$ 7.56	$ 7.56

Mechanics of Market Assistance Loans

There are only a few requirements for minor oilseed and pulse crops to qualify for marketing assistance loans. Producers must have current-year production of these crops in order to receive a marketing assistance loan. A commodity offered for loan must be of "loan" quality. Quality specifications for each loan commodity are available from Farm Service Agency offices. Producers must also fulfill USDA expectations specified in their conservation compliance plans for the management of highly erodible cropland to be eligible for marketing assistance loans.

Producers may place current year production under marketing assistance loans by self-certifying the quantity to be placed under loan up to 100 percent of current production. Producers must also certify that the current production to be placed under loan is of nonrecourse loan quality. The Farm Service Agency may spot check quality and quantity of the commodities that producers offer as collateral for marketing assistance loans.

Marketing assistance loans are available for a maximum of nine full months beyond the month loan proceeds are made available to a producer by the Commodity Credit Corporation (CCC). For example, a loan was issued on 2002 canola on November 2, 2002, then the loan had to be settled on or before August 31, 2003. If the loan was issued on November 27, 2002, the final settlement date would still be August 31, 2003.

There are several methods available for settling a marketing assistance loan. One method is to pay back the loan principal balance and accrued interest. (The rate of interest on marketing assistance loans is highly competitive with commercial interest rates). The commodity held as collateral is then released to the producer.

A second method for settling a marketing assistance loan is to forfeit the commodity held as collateral to the Commodity Credit Corporation. A producer is expected to deliver the commodity to a designated CCC receiving point. Costs incurred for the delivery of a commodity are the responsibility of the borrower. The forfeited collateral goes towards satisfying the loan balance and accrued interest. The forfeited commodity is subject to a discount and premium schedule. If the quality of the forfeited commodity is below quality standards, the borrower is expected to use cash to settle the loan. A producer is also be expected to use cash to complete loan repayment if the quantity of a commodity certified for loan exceeded that which the producer delivered for settlement. The cash payment makes up the discount for quality or the lack of quantity.

A third method available for settling marketing assistance loans is to repay a loan prior to maturity at the posted-county price and realize a marketing loan gain. This alternative is discussed in a subsequent section.

Background on Loan Deficiency Payments

Loan deficiency payments (LDPs) were authorized under the Food, Agriculture, Conservation and Trade Act of 1990. Starting with the 1991 crop, the loan deficiency payment mechanism was available to producers of oilseed crops. LDPs were rarely used until the late 1990s because prices for loan commodities were not low enough to trigger LDPs. When dry peas, lentils and chickpeas became loan commodities under the Farm Security and Rural Investment Act of 2002, the LDP eligibility was extended to dry peas, lentils, and chickpeas.

LDPs are available whenever the CCC-determined value of a commodity, also referred to as the *posted-county price,* is below the loan rate for a subject commodity. The posted-county price for a commodity is established by FSA by adding a commodity-specific differential to an appropriate terminal price. It appears that the county

differential is an approximation of shipping and handling costs between an interior market in a county and a pertinent terminal market(s).

Differentials applicable to the 2003 crop year for each minor oilseed crop in each Montana county are shown in Appendix B, Figures 8 through 14. In some Montana counties two differentials exist indicating at least two pertinent terminal markets for that commodity.

For pulse crops the specification of differentials is quite different than for oilseeds. The differential for dry peas for all Montana counties for 2003 production is -$0.79 per hundredweight. In FSA tables the reference to a terminal market is "US". There are no differentials specified for lentils or small chick peas although weekly posted-county prices are available for these pulse commodities.

Use of Differentials in the Calculation of LDPs

Differentials are used to calculate posted county prices. More specifically the equation is:

Posted-County Price = [Commodity Terminal Price] plus [Differential].

Differentials are expressed as negative values. Arithmetically, differentials are added to the terminal market prices to derive posted-county prices.

When two terminal markets are listed for a particular commodity both posted-county prices are calculated and the higher posted-county price is selected (See Appendix B, Figures 8 through 14, for minor oilseed commodity differentials).

A loan deficiency payment for a particular commodity is calculated as the difference between county loan rate for a commodity and posted-county price for a commodity. More specifically the equation is:

Loan Deficiency Payment = [Commodity Loan Rate] less [Posted-County Price].

County loan rates are set annually. Posted-county prices are set weekly for minor oilseed commodities and pulse commodities. Methods for determining LDPs are tractable. For minor oilseeds and pulse crops a unique LDP for each commodity is established each business week within the year that reflects weekly changes in relevant terminal prices. Posted-county prices for other oilseed and pulse crops are made known Friday of each week and prevail that day through Thursday of the following week.

Consider, as an example, canola in Cascade County on August 22,2003. The Velva, North Dakota, terminal price for August 22, 2003, was $9.94 per hundredweight. The differential for that market is -$1.69 per hundredweight. There is no other relevant terminal market for canola originating from Cascade County acknowledged by FSA (Appendix B, Figure 8).

The posted-county price calculation for August 22, 2003, was:

Velva: $9.94 + (-1.69) = $8.25.

This posted county price for canola in Cascade county prevailed through August 28, 2003. When there are two or more differentials assigned to a commodity within a county the largest posted-county price is considered when calculating LDP. The underlying assumption is that a producer would sell into the highest cash market.

Thus the posted-county price applicable for canola in Cascade County on August 22 was $8.25 per hundredweight.

The applicable 2003 canola loan rate for Cascade County is $8.60 per hundredweight, as shown in Appendix A, Figure 1.

The LDP calculation for this example is:

$8.60 -8.25 = $0.35.

In this example a producer with harvested and measurable 2003 canola could have received $0.35 per hundredweight as a loan deficiency payment on August 22. However, if a producer had elected to receive an LDP, the producer would have forfeited the opportunity to take a marketing assistance loan on that quantity.

Eligibility for LDPs

To be eligible for LDPs on loan commodities producers must have current crop year production. All producers having an interest in the crops produced are eligible for LDPs.

Producers must have beneficial interest in harvested commodities on the dates their LDPs are requested. In general beneficial interest means that a producer (1) maintained ownership, (2) is at risk, and (3) controls the movement of the commodity. In addition, the commodity must have been mechanically harvested and the commodity must be from the harvest of a current crop.

The final date each year to request an LDP on a commodity is the earlier of the loss of beneficial interest in the commodity or the final marketing assistance loan date availability for the commodity. For minor oilseed and pulse crops of interest in Montana, the final loan availability dates are either March 31 or May 31 following the harvest of crops in the previous fall. FSA offices have schedules of final dates for all loan commodities.

Other Considerations Relative to LDPs

Loan deficiency payments are taxable for income tax purposes. For instance, the $0.35 per hundredweight received for 2003 canola in Cascade County on August 22 will treated as ordinary income for income tax purposes.

If a producer elects to take out an LDP on eligible production of a minor oilseed or pulse crop, the producer is not allowed to obtain a marketing assistance loan on that production. Therefore, a producer needs to have in place a marketing plan that will provide a sales price per unit of production plus a per unit LDP that at least equals the marketing assistance loan rate for a commodity.

Producers retain their production when they take LDPs. If they pursue a strategy where they expect to receive storage price premiums when they sell a commodity, their commodity can be used as collateral to obtain a commercial loan to fulfill short term cash flow needs.

Finally, producers must remain cognizant that LDPs are only available when market prices are relatively low such that posted-county prices for a commodity are less than its county-level loan rate.

Marketing Loan Gains

Marketing loan gains have existed in concept since authorized under the FACT Act of 1990. Starting with the 1991 crop, the marketing loan gain mechanism was available to producers of minor oilseed crops. Marketing loan gains were uncommon prior to the late 1990s because commodity prices had not been sufficiently low to trigger marketing loan gains. Marketing loan gains for dry peas, lentils and small chickpeas were first authorized for the 2002 crop year.

A marketing loan gain is sometimes available prior to loan maturity for a producer who took a marketing assistance loan. In order for there to be a marketing loan gain, the CCC-determined value of a commodity (the posted-county price) has to be below the loan rate at the time of settlement of a marketing assistance loan. Under certain circumstances a marketing loan gain can be "locked in" for up to 60 days.

Marketing loan gains are available for commodities under a marketing assistance loan (CCC loan) that are (1) to be delivered to a buyer by the loan repayment date or (2) repaid with cash by the loan maturity date.

A marketing loan gain is defined as:

Marketing Loan Gain = [Commodity Loan Rate] less [Posted-County-Price].

Consider the following example. The 2002 county-level loan rate for canola in Cascade County in 2002 was $ 8.51per hundredweight. A producer obtained a loan on 2002 canola production on November 2, 2002. The producer needed to settle the 2002 crop year marketing assistance loan by August 31, 2003. The producer decided to settle the loan on August 28, 2003. On that day the posted-county price for canola in Cascade County was $8.25 per hundredweight.

The marketing loan gain was:

$8.51 - 8.25 = $0.26 per hundredweight.

This producer was able to reclaim the canola used as collateral for $8.25 per hundredweight, consequently gaining $0.26 per hundredweight on every hundredweight under loan. The gross revenue of the canola will be the market value from the sale of the canola plus the $0.26 marketing loan gain realized on August 28.

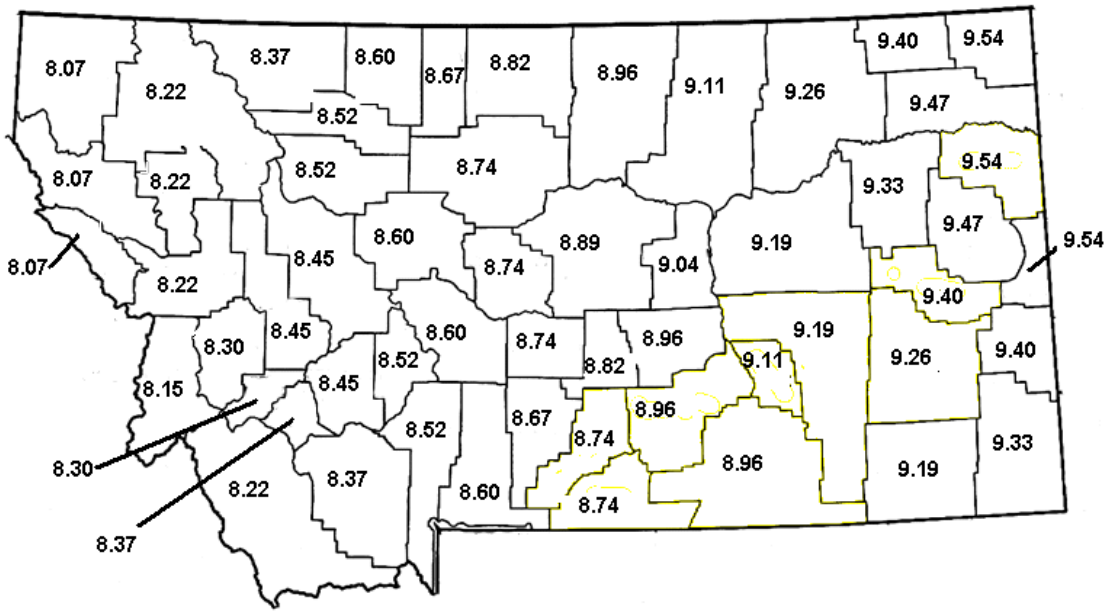
To summarize, marketing loan gains occur at loan settlement. A marketing loan gain, when available, can

be taken by a producer any time during the interval from loan issuance to loan maturity. Marketing loan gains may be the preferred method to settle marketing assistance loans when commodity prices are relatively low compared with loan rates. A producer who consider taking a marketing loan gain is attempting to realize total revenue from the sale of a commodity plus a marketing loan gain that is at least greater than the loan rate for the commodity.

Producers who settle a marketing assistance loan by taking a marketing loan gain will have accrued interest forgiven. For income tax purpose, the marketing loan gain must be reported as taxable income, but accrued interest forgiven on a nonrecourse loan is not reported as income.

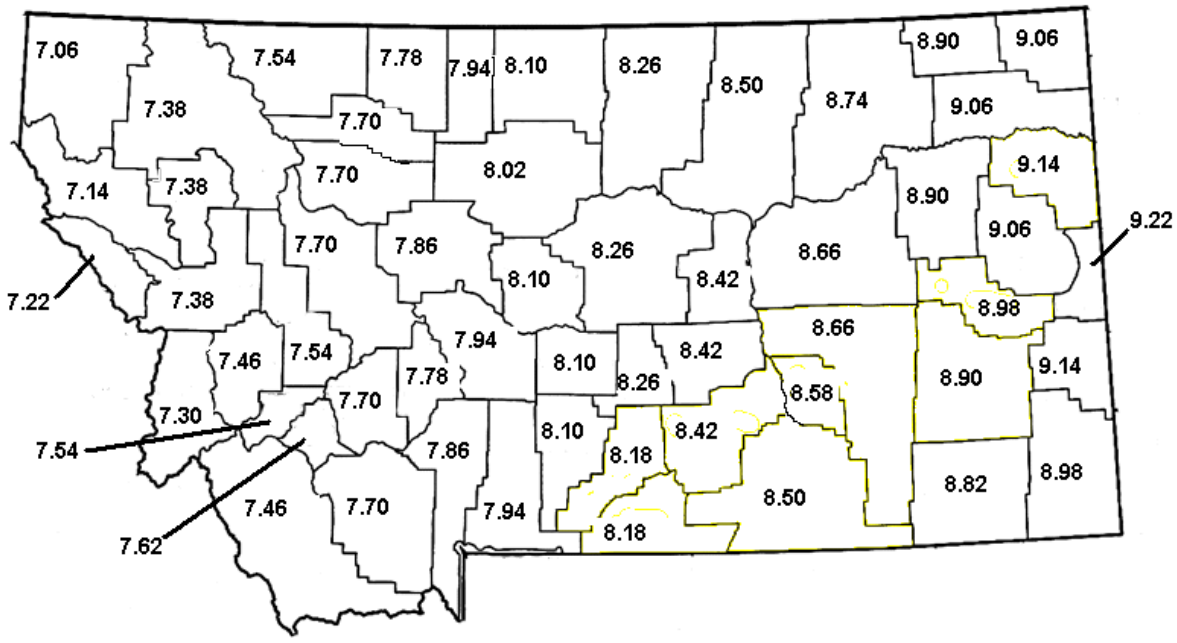
Appendix A: County-Level Marketing Assistance Loans

Figure 1: County-Level Marketing Assistance Loan Rates for Canola, 2003 Crop Year ($ Per hundredweight*)



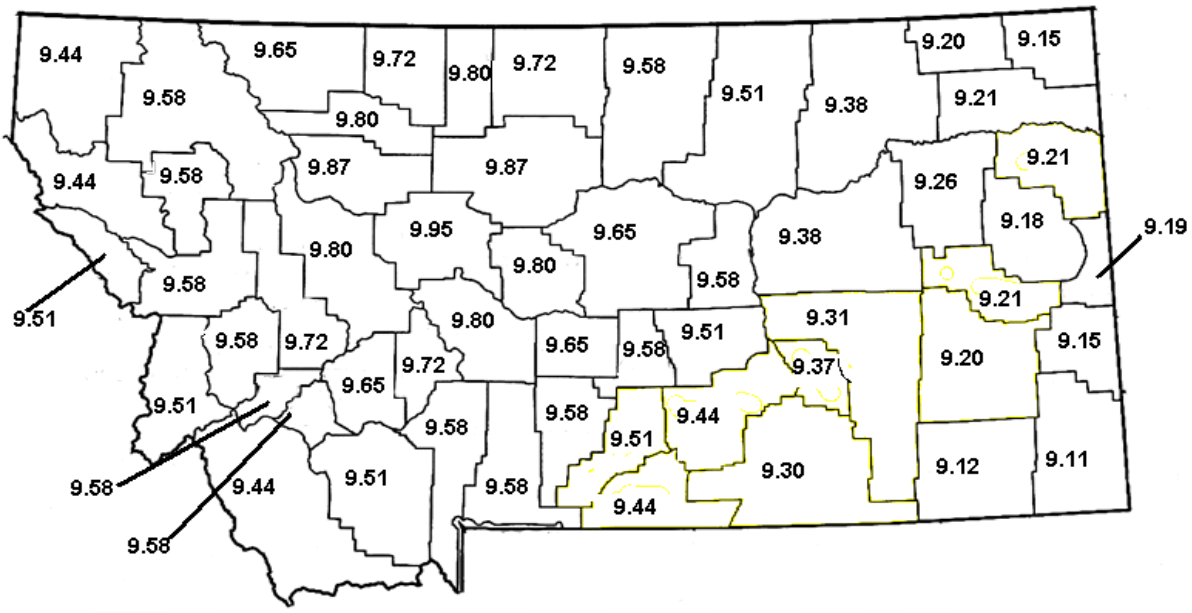
*The presence of a loan rate does not imply that the crop is agronomically well-suited.

Figure 2: County-level Marketing Assistance Loan Rates for Crambe, 2003 Crop Year ($ per hundredweight*)



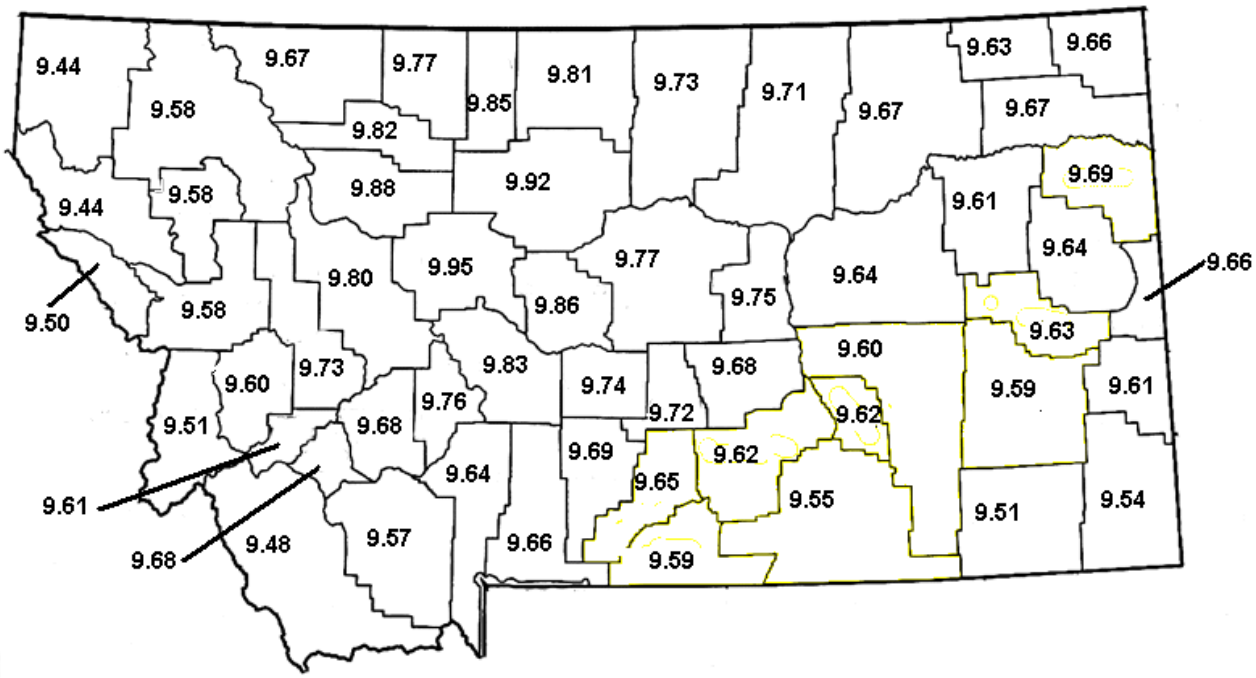
* The presence of a loan rate in a county does not imply that the crop is agronomically well-suited.

Figure 3: County-level Marketing Assistance Loan Rates for Flaxseed, 2003 Crop Year ($ per hundredweight*)



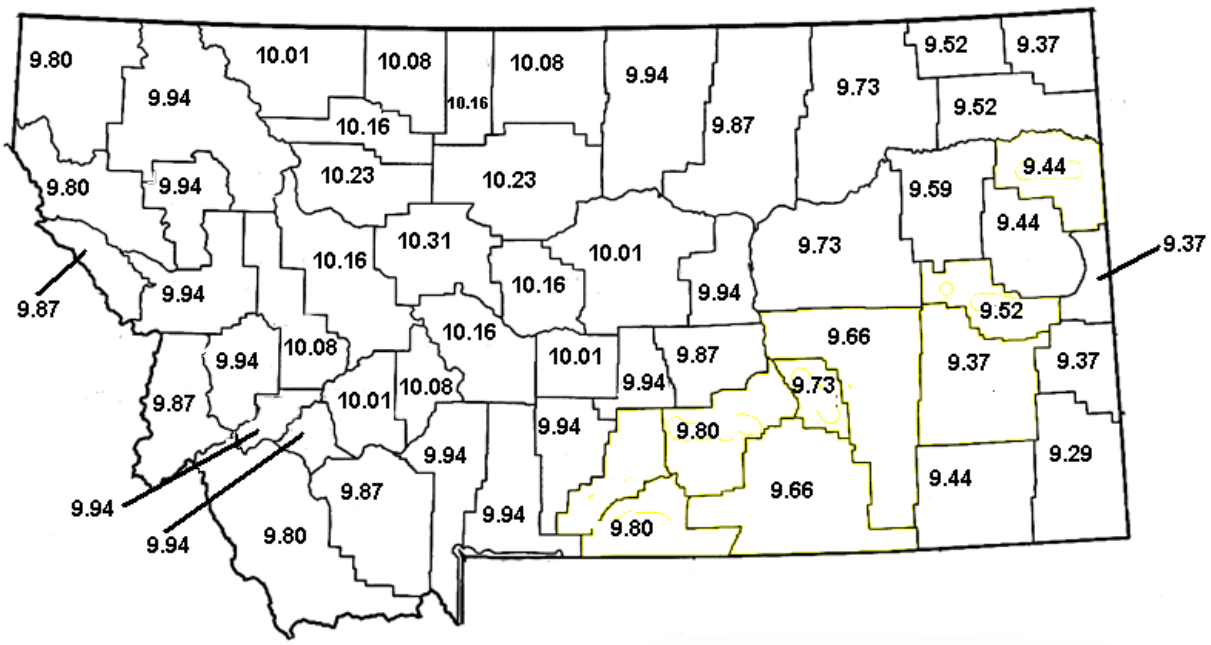
* The presence of a loan rate in a county does not imply that the crop is agronomically well-suited.

Figure 4: County-level Marketing Assistance Loan Rates for Mustard, 2003 Crop Year ($ per hundredweight*)



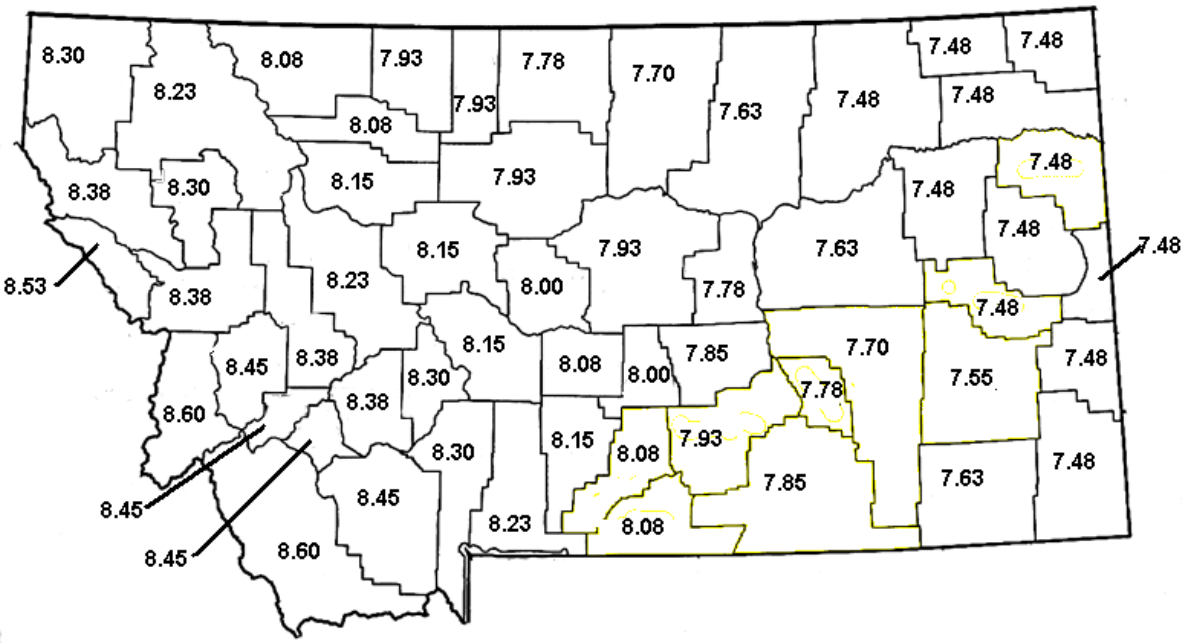
* The presence of a loan rate in a county does not imply that the crop is agronomically well-suited.

Figure 5: County-level Marketing Assistance Loan Rates for Rapeseed, 2003 Crop Year ($ per hundredweight*)



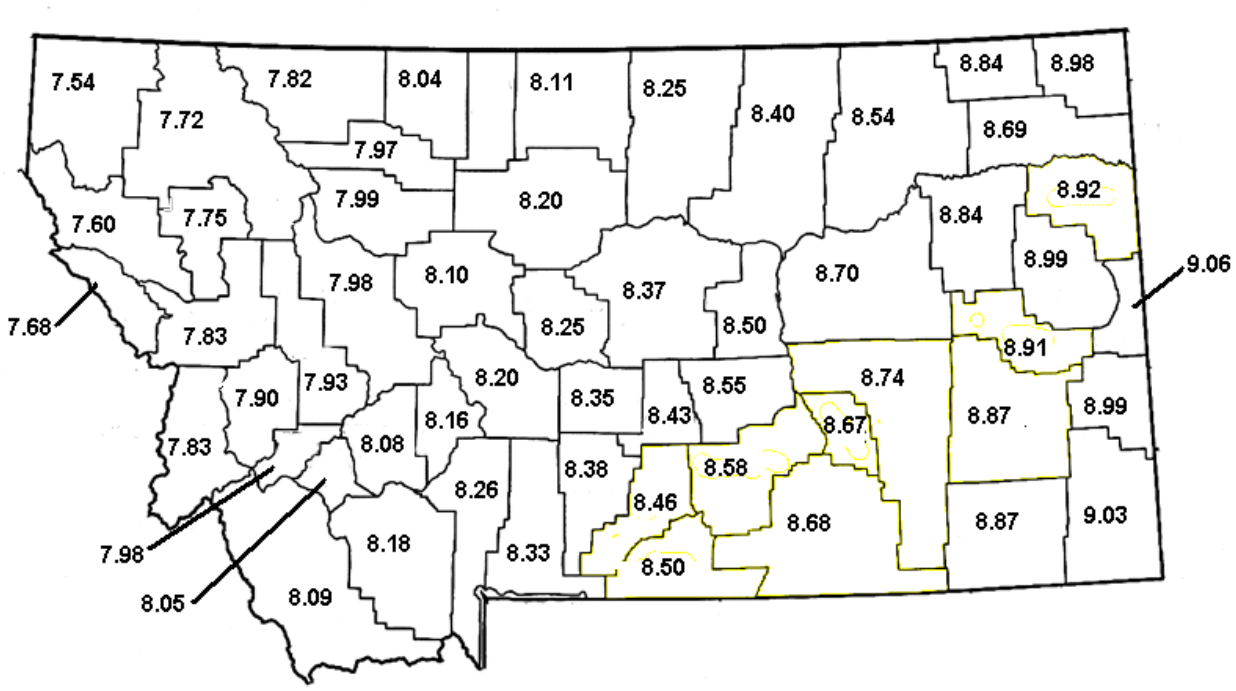
* The presence of a loan rate in a county does not imply that the crop is agronomically well-suited.

Figure 6: County-level Marketing Assistance Loan Rates for Safflower, 2003 Crop Year ($ per hundredweight*)



* The presence of a loan rate in a county does not imply that the crop is agronomically well-suited.

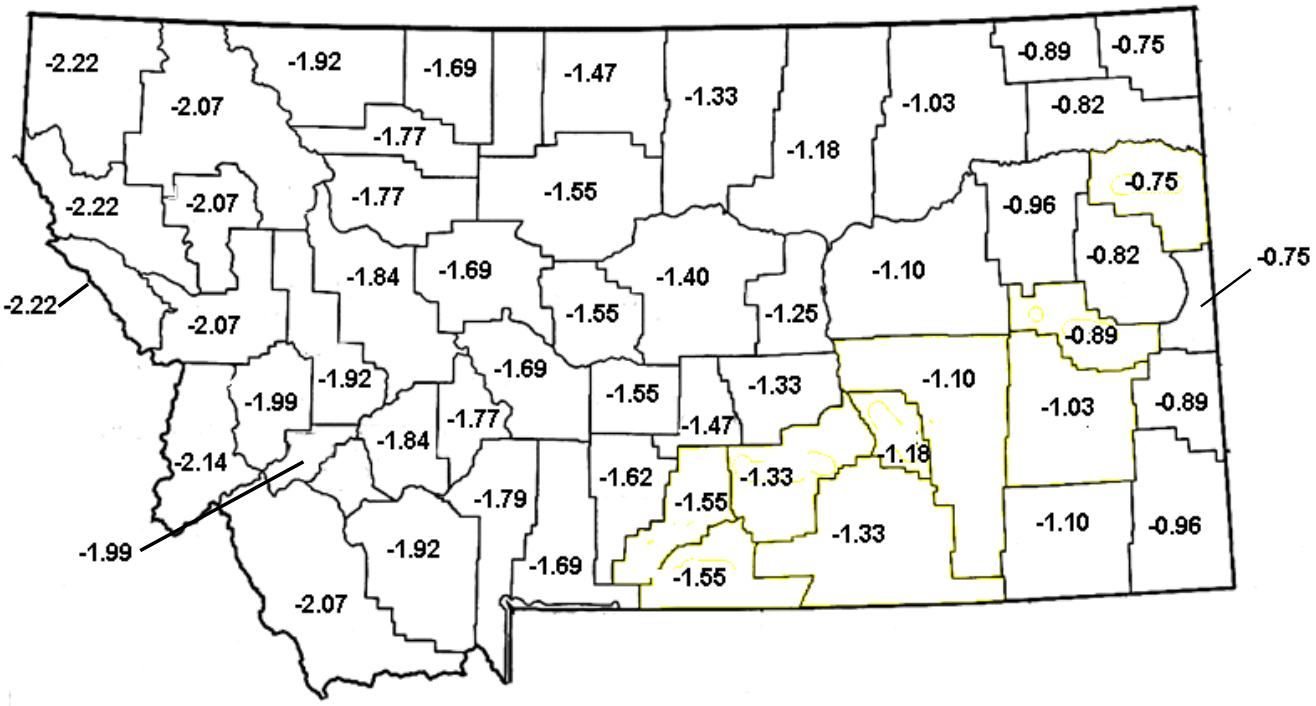
Figure 7: County-level Marketing Assistance Loan Rates for Sunflower, 2003 Crop Year ($ per hundredweight*)



* The presence os a loan rate in a county does not imply that the crop is agronomically well-suited.

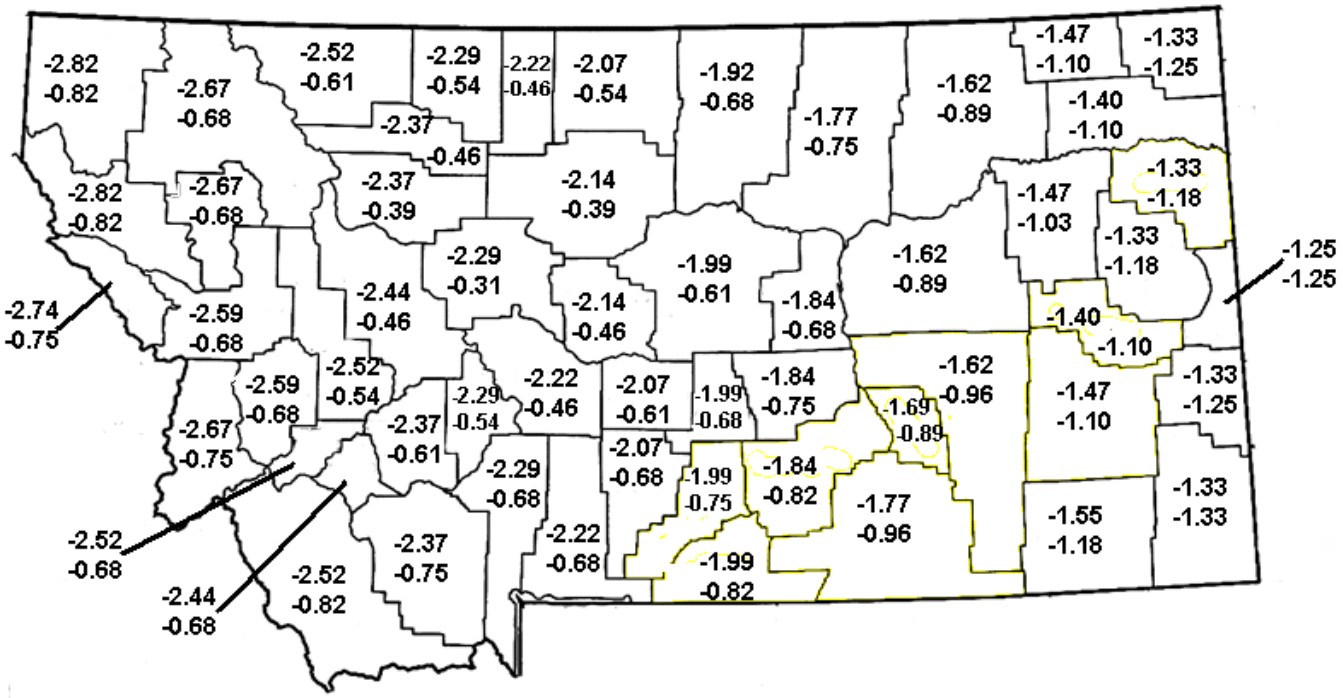
Appendix B: Differentials, by Terminal Markets, for Minor Oilseed Commodities

Figure 8: Canola Differentials for 2003 Crop Year ($ per hundredweight*)



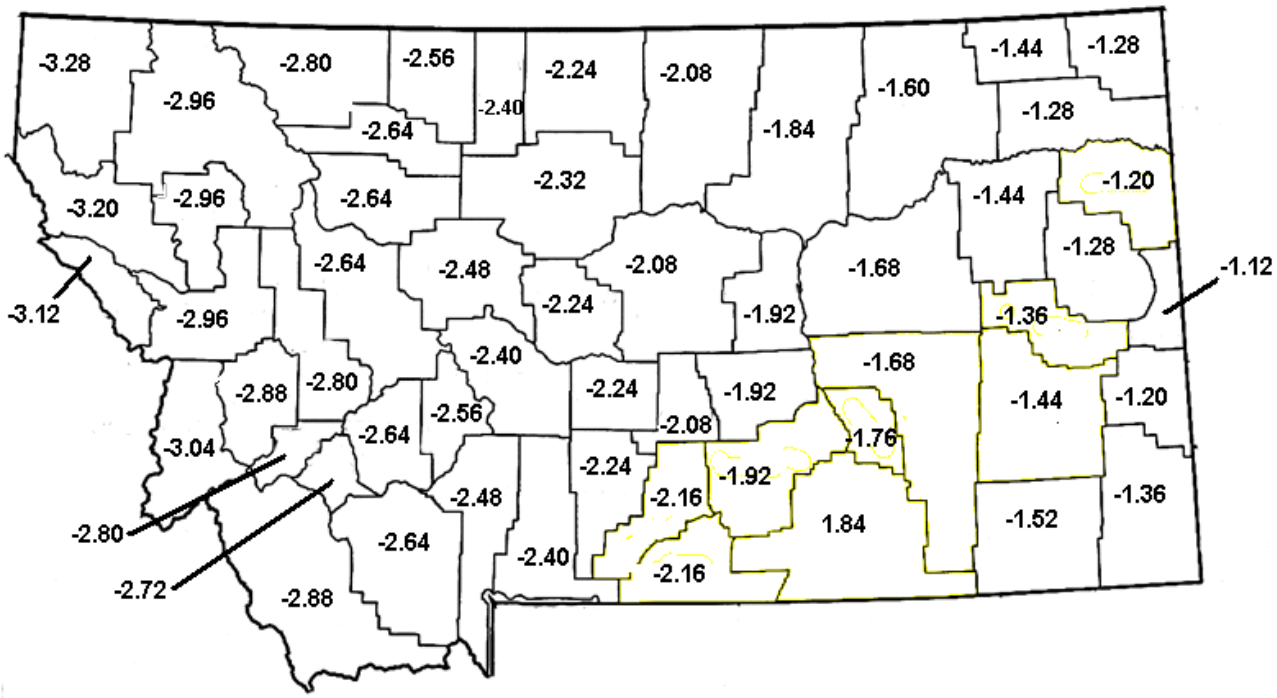
* Velva, North Dakota is the reference terminal market for canola.

Figure 9: Crambe Differentials for 2003 Crop Year ($ per hundredweight)*



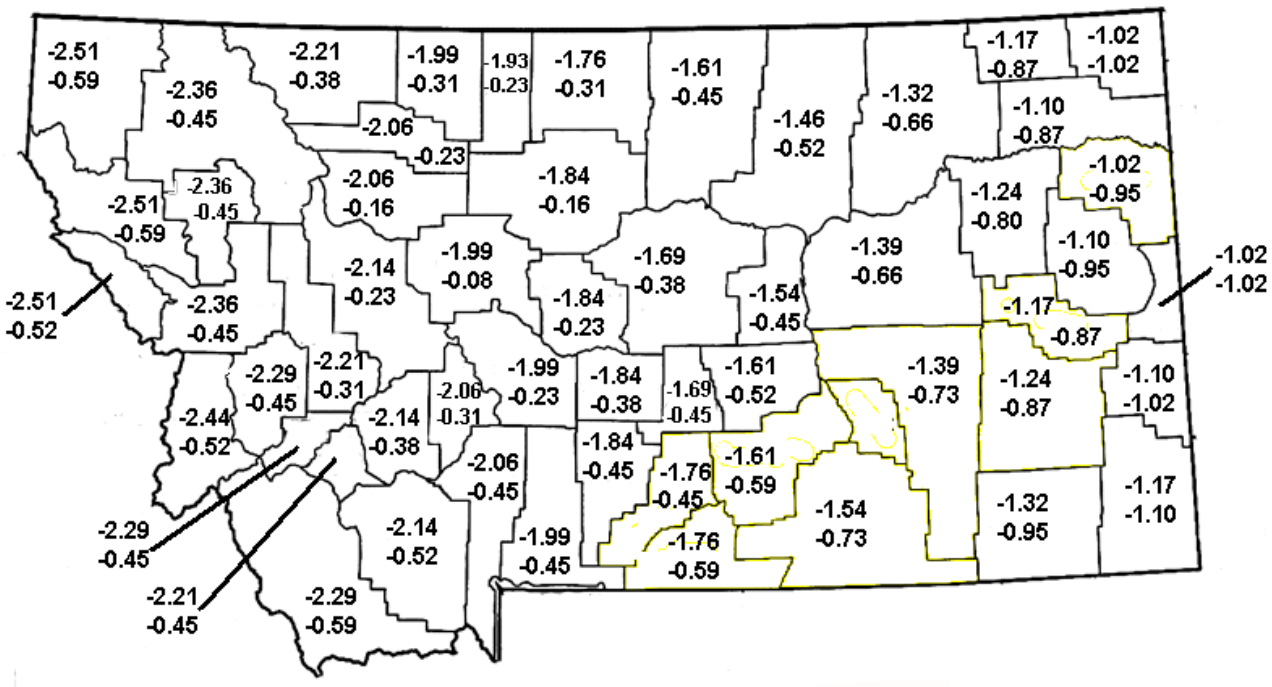
* Fargo, North Dakota is the terminal market with the top listed differential.
* Great Falls, Montana is the terminal market with the bottom listed differential.

Figure 10: Flaxseed Differentials for 2003 Crop Year ($ per hundredweight*)



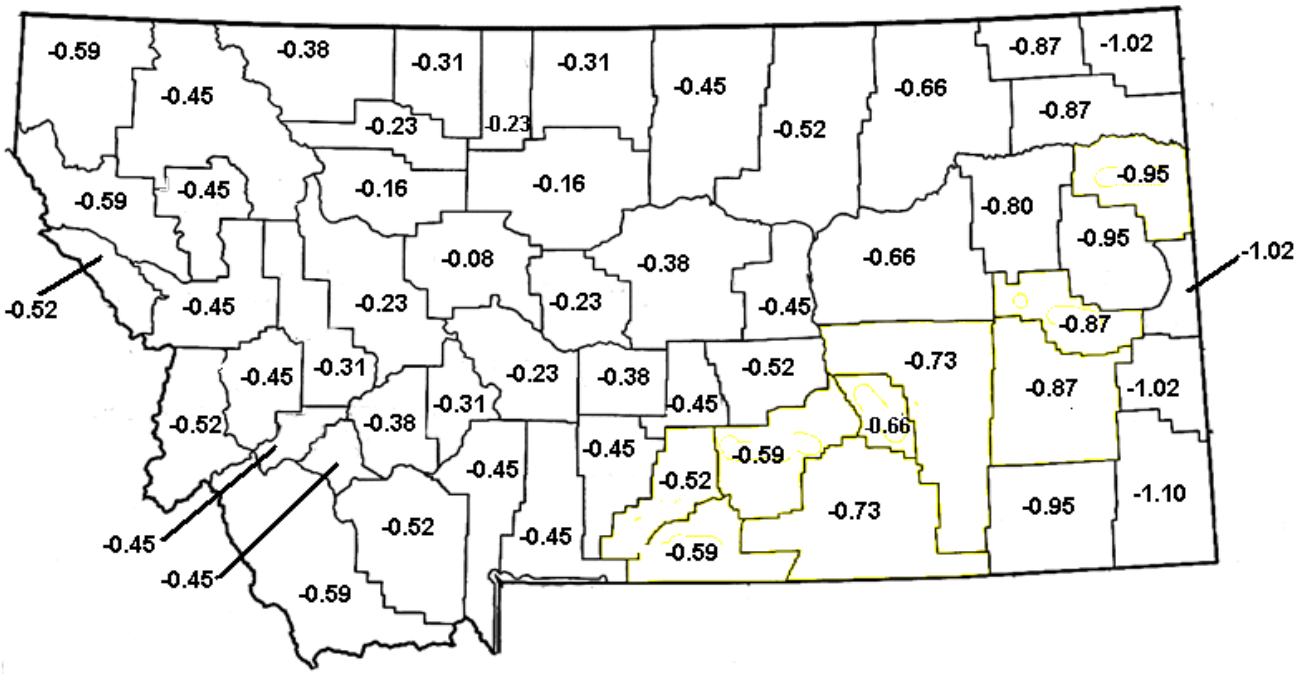
* Carrington, North Dakota is the reference terminal for crambe.

Figure 11: Mustard Differentials for 2003 Crop Year ($ per hundredweight*)



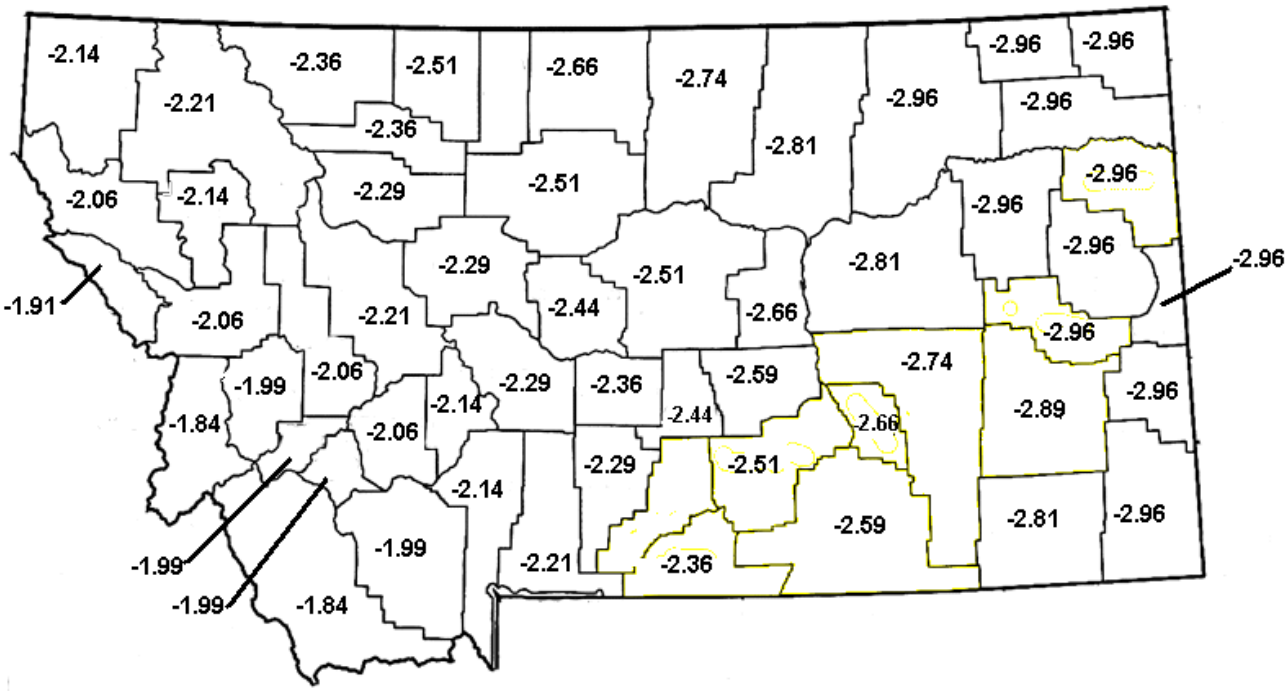
* Grand Forks, North Dakota is the terminal market with the top listed differential.
* Great Falls, Montana is the terminal market with the bottom listed differential.

Figure 12: Rapeseed Differentials for 2003 Crop Year ($ hundredweight*)



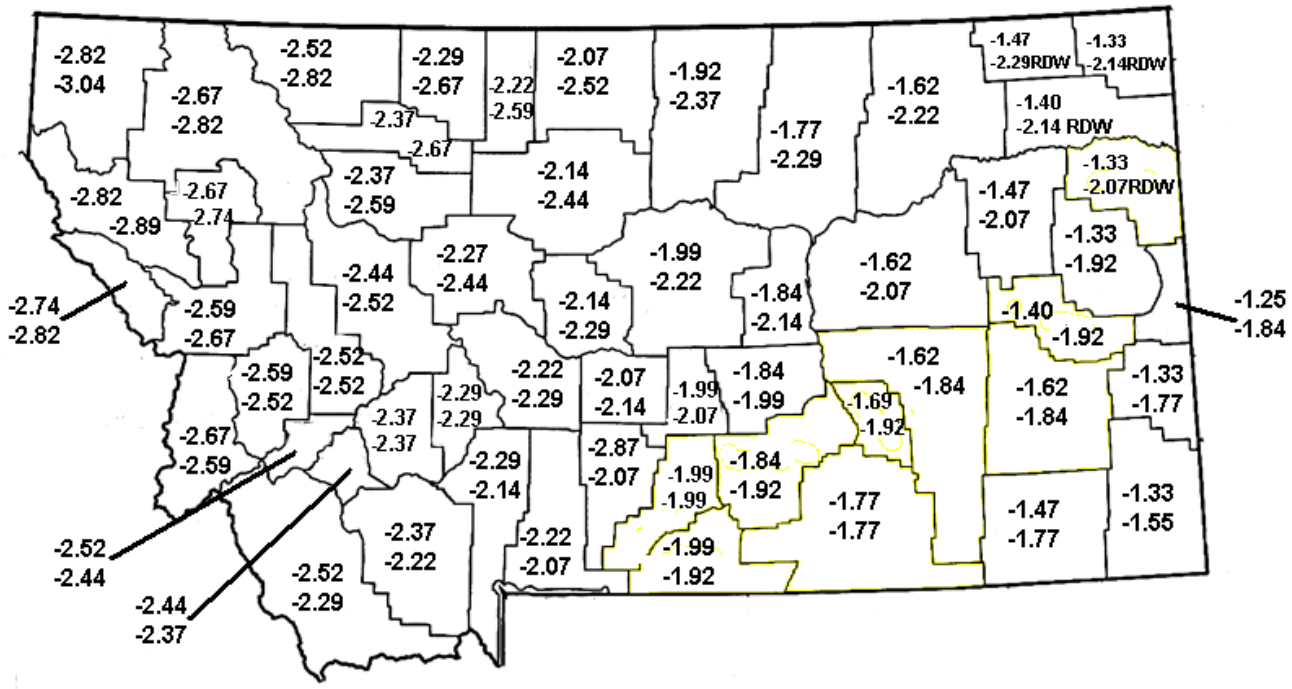
* Great Falls, Montana is the reference terminal market for rapeseed.

Figure 13: Safflower Differentials for 2003 Crop Year ($ per hundredweight*)



* Culusa, California is the reference terminal market for safflower.

Figure 14: Sunflower Differential for 2003 Crop Year ($ per hundredweight*)



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