



# Ag Decision Maker



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## Modest Gains for Cash Rental Rates

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**A**verage cash rental rates in Iowa have increased modestly over last year, according to results from an annual survey by Iowa State University. Forty percent of Iowa's cropland is rented under cash rent lease agreements. Profits and losses are highly variable from year to year, and expectations of future returns ultimately are bid back into land rents as well as land selling prices.

A year ago both landowners and tenants were anticipating a surge in cash rents resulting from larger government payments under the 2003 farm bill. However, yields and prices have probably had more impact on rental rates for this year than the new USDA program.

by giving their best estimates of typical cash rental rates in their county. Cropland in each county was divided into high, medium and low quality thirds based on expected corn yields. Data also were collected for oats, hay and pasture land rents. They showed little change from past years.

It is difficult to tell how much impact the new farm bill had on cash rents for 2003. Expectations of higher USDA payment levels have largely evaporated, as grain prices have remained above loan rates most of the year. It appears that farmers will not collect loan deficiency payments or counter cyclical payments for the 2002 crops.

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### Survey Results

The ISU survey of cash rental rates for 2003 showed increases in typical cash rents for all regions of the state. The largest increases were in east central and southeast Iowa. The estimated average rental rate for the entire state was \$128 per acre, compared to \$124 last year. Most counties showed modest increases in typical rents, especially for lower quality land.

A total of 1,121 farm tenants, land owners, real estate agents, farm managers, and lenders responded to this year's survey,

### Handbook Updates

For those of you subscribing to the *Ag Decision Maker Handbook*, the following updates are included.

**Corn and Soybean County Yields** — File A1-14 (4 pages)

**2003 Farmland Cash Rental Rates** — File C2-10 (13 pages)

Please add these files to your handbook and remove the out-of-date material.

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That leaves only the direct payments to supplement income from the marketplace. On the positive side, new records were set for state average yields in 2002, and many farms harvested their best crops ever. While prices are not at high levels, they have risen enough to offset the loss of loan deficiency payments in most counties. Moreover, strong competition for rented land has kept rates at historically high levels in many communities.

Rents Vary by Productivity

Average rents per bushel of expected corn yield were calculated using county average yields since 1993. These rates ranged from about \$.87 per bushel in south central Iowa to over \$1.00 per bushel in east central Iowa. Stronger grain prices near the Mississippi River and the large number of acres devoted to seed production tended to support rental rates in some areas.

The full summary of the survey is contained in the accompanying Decision File 2003 Farmland Cash Rental Rates, File C2-10.

Negotiating Individual Terms

Not all lease agreements will follow the trends. There are two basic approaches to negotiating rental rates. Some tenants and owners attempt to

adjust the rent yearly, to reflect near-term economic prospects or results. Other leases, especially long-term agreements between the same parties, are adjusted infrequently on the assumption that high and low profit years will even out over time.

Individual lease agreements will vary considerably from average rates. Particular farms may include areas that have poor drainage or are highly eroded, or that are low in fertility. Other farms may have small or irregular fields, or terraces to work around. The size of the USDA corn base and program yield associated with a particular farm affects the value of the direct and counter cyclical payments received. All of these factors influence the level of rent tenants are willing and able to pay.

Local grain market conditions, the availability of seed or specialty grain contracts, and the number of rental acres available also cause rental rates to be higher or lower in certain communities. The information shown in this survey can be used to benchmark rates among counties, and to indicate trends, but should not substitute for careful consideration of expected costs and returns as a basis for negotiating terms for a specific parcel of land.

Country of Origin Labeling \*

by Roger A. McEowen, Associate Professor of Agricultural Economics and Extension Specialist, Agricultural Law and Policy, Kansas State University.

The Country of Origin Labeling (COOL) provisions in the 2002 Farm Bill require, beginning September 30, 2004, that retail sellers of certain food commodities inform consumers of a product's country of origin. As required by the statute, the USDA promulgated guidelines in the fall of 2002 designed to assist retailers and their suppliers in facilitating voluntary labeling. By September 30, 2004, however, the USDA is to have in place regulations implementing mandatory COOL. COOL raises important questions concerning what commodities are covered, how the labeling requirement is satisfied, and anticipated costs and benefits.

wild), peanuts, fruits and vegetables. Covered commodities must be exclusively produced and processed within the United States to be deemed of U.S. origin. Retailers of these statutorily defined commodities must inform consumers as to country of origin. Farmers, ranchers, growers and fisherman are not specified as a "covered entity" by the text of the statutory language and, as a result, are not within the purview of the statute, because they do not prepare, store, handle or distribute relevant covered commodities (at least as to meats).

Satisfying the Statutory Requirement

The COOL legislation regulates private-actor conduct through an information requirement and a verification requirement. The information

"Covered Commodities"

"Covered commodities" are defined by the statute as beef, pork and lamb in the form of whole muscle cuts and ground meat, fish (farm-raised or

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requirement mandates that retailers inform consumers as to country of origin of a covered commodity. The method by which consumers are to be notified is through a “label, stamp, mark, placard,” or other type of signage that is “clear and visible” at the point of sale. Retailers are exempt if they purchase for sale at retail less than \$230,000 per year of fruits and vegetables or of all covered commodities. Food service establishments, such as restaurants and cafeterias, are exempted from the information requirement.

The statute also contains a verification requirement specifying that “any person in the business of supplying a covered commodity to a retailer shall provide information to the retailer indicating the country of origin of the covered commodity.” Thus, the statutory language clearly imposes a duty only on *direct suppliers* to retailers rather than on all upstream suppliers.

Importantly, the verification requirement merely vests *discretionary* authority in the Secretary of Agriculture to require handlers, processors or distributors of covered commodities to maintain a verifiable recordkeeping audit trail. The Secretary is statutorily prohibited from imposing a *mandatory* identification system to verify country of origin. However, it appears from the USDA guidelines that the Secretary fully intends to require such an audit trail. An important point is that while the Secretary may write regulations necessary to implement COOL, it remains highly questionable whether the regulations could govern livestock producers. Livestock (such as cattle and hogs) are not “covered commodities” as defined in the statute.

**COOL Enforcement Mechanisms**

Retailers that “willfully” violate the law are subject to a fine of up to \$10,000 per violation. However, the fine may not be assessed unless the Secretary has provided the retailer with a notice of a suspected violation and a 30 day opportunity to correct the problem. In practice, this means that a retailer is not to be held liable for negligent violations, or innocent mistakes. For covered entities that are not retailers, the enforcement provisions contained in the Livestock Mandatory Reporting Act of 1999 apply. The Secretary must consider several factors before issuing a fine including “the gravity of the offense, the size of the business involved, and the effect of the penalty on the

ability” to continue in business. Though the standard for issuing a fine differs here from the retailer standard, it is likely that the Secretary will require a finding akin to willfulness before levying a fine. There appears to be no legitimate reason to treat different (by type) covered entities in an inconsistent manner under the enforcement regime.

**COOL Costs – The Recordkeeping Burden**

If the USDA promulgates final rules implementing mandatory COOL that specify that the verification requirement be met via an audit trail, the lack of competitive agricultural markets (particularly in livestock) creates the potential for the COOL requirements to be pushed downstream to individual producers. Even so, it is unlikely that any additional producer recordkeeping will be needed to establish origin beyond the records that producers maintain presently. While the USDA guidelines require records to be maintained for two years, it seems unlikely that additional records would need to be maintained beyond those maintained presently for tax, animal health, livestock births, animal and feed purchases, sales, and inventory purposes.

The recordkeeping burden for handlers can also be expected to be minimal. All importers are required presently to maintain records on the country of origin of imported products pursuant to existing customs regulations. The dominant food handling firms (packers, processors, wholesalers and distributors) are the ones most likely to procure from multiple sources, including U.S. and foreign origin. It is these dominant firms that the recordkeeping burden will affect the most.

While retailers are required to provide information to consumers as to the country of origin of covered commodities, retailers currently maintain detailed records as to purchases and sales that can be expected reasonably to satisfy auditors charged with verifying labeling claims.

It appears unlikely that mandatory COOL will require an elaborate new system of recordkeeping in light of the volume of information that buyers and sellers share presently. Information concern-

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ing a product's origin can be placed on a bill of lading, invoice, affidavit or on any standardized form, and can be incorporated into information that is presently maintained for other purposes. Implementation of mandatory COOL could also be aided by the USDA utilizing a presumption of U.S. origin designed to focus a monitoring system only on products that are required to pass through customs, instead of on all products, including those of U.S. origin.

**COOL Benefits**

A study regarding consumer willingness to pay for beef labeled as to country of origin was conducted by researchers at Colorado State University and the University of Nebraska-Lincoln and released

on March 20, 2003. Entitled "Country of Origin Labeling of Beef Products: U.S. Consumers' Perceptions," the study surveyed consumers to determine their willingness to pay for meat labeled as U.S. origin. The researchers found that the vast majority of consumers (73 percent) in Denver and Chicago were willing to pay an 11 percent premium for steak and a 24 percent premium for hamburger that is labeled as to country of origin. An actual auction determined that consumers were willing to pay an average of 19 percent more for steak labeled "Guaranteed USA: Born and raised in the U.S." Those results indicate that COOL could bring substantial benefits to the agricultural sector in general, and the livestock sector in particular.

**Quality Management Systems for Grain Markets**

*by Charles Hurburgh, Jr., Chair, Ag Quality Initiative, and professor of agricultural engineering*

*(Second in a series of two)*

Recent security concerns have lead many to believe Quality Management Systems (QMS) are needed to provide trace-ability, chain-of-custody, and security against food supply threats even in basic staple commodities. There are two routes by which QMS are being introduced at the local level through normal grain markets (that are often owned by producers), and through producer-held companies created to develop markets and coordinate very specialized production.

**Development Process – Grain Handler Driven**  
Several grain companies are developing internal quality management systems. There are examples of International Organization for Standardization (ISO) certification such as Colusa Elevator Company, Consolidated Grain and Barge, Inc., and of other systems such as American Institute of Baking Quality Systems Evaluation (AIB QSE) such as Farmers Cooperative Elevator Company, Farmland Industries.

Firms that have an audited quality management system are good candidates for direct marketing arrangements – producer to end-user. Transportation and logistics have often prevented direct sales of bulk products; the firms creating source verification are becoming large enough that coordina-

tion of source verified bulk shipments is much more feasible than in the past.

In the grain industry program, source verification was divided into nine general areas, and specific procedures/controls were created for each.

- Raw Materials
- Process Control
- Process Verification (Statistics)
- Finish Product Acceptability
- Storage and Shipping
- Instrument Accuracy and Calibration
- Personnel Training
- Plant Programs (Safety, etc)
- Quality Policies (Management Commitment)

At this time, there is not an active specialty grain market; the benefits and targets are all based on commodity corn and soybeans. However, some firms are in an excellent position to discuss specialty needs, such as non-GM or other attributes on a larger scale basis than individual producers might be able to offer.

Part of grain handling source verification is the tracking of product from receipt to resale or use. This is important if a special trait is involved, and even more so if some consumer health or safety



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issue is involved. Logically grain handlers will extend the QMS process back to the producer in measured steps working backward from the scale ticket (receipt document of delivery). A gradual progression of activities moving back from delivery will bring producers to the level for certification without impressing major work with little tangible value to offer in exchange. QMS are essentially people training and interaction activities, such as:

- Identify wagons and trucks, and record container, time and date of deliveries. This would extend trace-ability to a field or bin if needed.
- Determine if pre-delivery sampling and control of delivery timing could improve off-harvest merchandizing potential and minimize inventories of off-grade grain.
- Utilize agronomy sales departments to create interaction with producers about data management, possible economies for them, and actual data collection in cases where the grain company is the primary input supplier.
- Document completely the use of company supplied inputs by producers.
- Develop an in-company standard data management/documentation protocol to be applied (and trained to) when and if there is a market need requiring QMS and trace-ability.
- When premium opportunities exist, always attach some QMS activity requirements to the premium. For a bulk handler, premiums are likely to be incremental at first.
- Incremental value traits (such as feed ingredient modifications or bulk non-GM) are best suited to grain handler organized QMS.

Development Process – Producer Supply Network Producers organized to form supply network companies have some advantages in the initial stages of specialty grain production and QMS establishment. Member’s investment in these companies makes the creation of a full QMS system easier to achieve. Time investments are made to support the financial commitments. Investors in these companies, while targeting high-value premium grains, are more likely to also recognize operating efficiencies that present themselves in the course of creating a full system QMS. The intangible time-based learning activities are more easily accepted in the investor-owner format. Owner-operators can also benefit

from promoting the idea “dealing with the grower”.

Producer networks lack distribution and logistics capabilities. The capital required for marketing to sophisticated users may be hard to obtain. Traits of smaller incremental value will be difficult to administer in this format. Therefore it will be very important for producer networks to understand their strengths and target products carefully.

- Producer networks will likely target higher value products, and those needing field research to commercialize.
- There are opportunities to identify cost savings in commodity operations, as well as specialty products.
- Initially there may be excess documentation, until confidence is established.
- Purity will be a major concern for the products of producer networks; operations affecting purity will be controlled even in commodity grain.
- Producer networks will maintain their individually strategic plans, but will utilize standard formats, templates and study guides for their certification programs, each applying those elements most relevant to the particular product involved.
- Technical expertise will be needed; any network must have at least one skilled person on staff.
- There will be opportunities with smaller incremental premiums where the high-value skills/procedures of a producer network connect with grain handler programs (such as sale of non biotech soybeans).

This concept is essentially an extension of the organic and container markets now operating for premium soybeans. The addition of increasing food safety and consumer concerns will impress more rigorous documentation and structure, such as is offered by QMS, but these markets will readily adapt to source verified QMS. The key addition will be third party audit and verification.

There are several groups in Iowa, that are organizing themselves in this way, or are upgrading their already successful organizations to more formal source verification.

**The Importance of the Grain Buyer in Source Verification**

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To capture the market benefits of source verification, the buyer must see value in the closer contact and chain-of-custody documentation that will exist. Some actions that only buyers can impress are:

- Give and demand integrity in all negotiations
- Provide simple, clear, complete and operationally feasible contract terms with reasonable economics
- Understand and interact with those actually capable of actually producing the product and bypass unneeded negotiators. Repetitive merchandising generally destroys source verification.
- Assume that the physical distribution system can do more than expected.
- Provide clear economics so that the market can pass costs and incentives efficiently. Market practices and baselines change with economic signals but respond poorly to wide ranging demands based on unclear economics.

Source verification and audited quality management systems are opening new direct market channels that require much more openness and

transparency.

**Third Party Audit**

All source verification systems require audit by disinterested third parties. Auditing services are being created. Among them, USDA is now deciding whether it should become a quality management system auditor, most likely to the ISO 9000-2000 standards.

**Summary**

Producers and grain handlers in Iowa are national leaders in developing source verification programs for grain. These programs allow close contact between producer and user, and provide quality assurance to meet consumer product and safety demands. Source verification requires detailed, documented and audited quality management systems. Direct supply of products in quantities previously thought not feasible will be enabled by source verification.

States themselves are not grain growing boundaries but they can be centers of thought and creativity. Source verification and customer service are people issues, not geography issues which means that choice of purchase sources can and will provide benefits.

**... and justice for all**

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