USDA narrowing differences with insurers over new crop insurance terms

By Agri-Pulse Staff

Washington, Feb. 18 –USDA's Risk Management Agency (RMA), which administers the Federal crop insurance program, yesterday revealed important elements of the second draft of a proposed new Standard Reinsurance Agreement (SRA), which establishes the terms, roles, and responsibilities for both the USDA and insurance companies that participate in the Federal crop insurance program.

The administration's original proposal would have cut crop insurance programs by $8.4 billion over 10 years, a move that farm state lawmakers like House Ag Committee Chairman Collin Peterson (D-MN) argued would not only reduce vital coverage, but reduce the farm bill baseline when the next farm bill is written. The new proposal instead would cut the program by $6.9 billion over 10 years. The new draft includes a series of significant changes, including many discussed during negotiations between the RMA and the participating crop insurance companies.

RMA data shows that annual insurance industry payments have doubled from $1.8 billion in 2006 to an estimated $3.8 billion in 2009 based on the terms of the existing SRA. Meanwhile, the number of total policies dropped slightly from 1.3 million in 2000 to 1.1 million in 2008.

The administration says it is attempting to cut the costs of subsidies to crop insurance companies and agents for delivering crop insurance coverage. National Crop Insurance Services Chairman Bob Parkerson said the change is a step in the right direction, but "we aren't there yet."

RMA Administrator Bill Murphy said Wednesday that he expects the insurance companies to continue to seek more concessions from USDA and "that's what the next round of negotiations I'm sure will key in on" over the next month.

Murphy explained that in USDA's new draft, "we've moved toward the directions that the companies have really requested." He said that in the negotiations over a new SRA, "about 90 percent of the companies said that they wanted more risk, both upside and downside, than we had provided in the first draft." He said that in the negotiations, USDA "went back and forth with the companies over the reasonable rate of return" and raised it in the second draft from 12% to "closer to a 14% return on retained premiums."

Overall, Murphy explained, USDA's "rebalancing" objective is to "reduce the gains in the main corn and soybean states in the Midwest and increase the gains in the other states" to increase the national coverage provided by the crop insurance program. He said the second draft responds to the companies' contention that "there was not enough gain opportunity in the non-corn/soybean states" versus the corn/soybean states "where they make most of their profits."

Also in response to insurance industry concerns, Murphy said that the latest draft proposes a revised quota share, up from the current 5% but down from the first draft's 10% to 7.5%. He said 2.5% of the new quota share "would be given back to the companies" by increasing USDA's subsidies for companies operating in or expanding into underserved states such as Nevada, Wyoming, Hawaii and Northeast states.

"The federal crop insurance program has served farmers well for many years and is an important part of the farm safety net," Agriculture Secretary Tom Vilsack said Wednesday. "We must maintain producer access to critical risk management tools and provide reliable protection from losses, while ensuring that we're taking appropriate steps to protect the interests of taxpayers. This second draft demonstrates USDA's commitment to responding to the concerns of the insurance companies in a way that meets USDA's original objectives. Today's announcement represents a significant step toward an agreement that will give us a stronger federal crop insurance program that helps producers manage risk, reduces volatility for crop insurance companies, serves farmers in every region of the country, and responds to taxpayer concerns."

The 2008 Farm Bill authorized USDA's Risk Management Agency, which manages the Federal Crop Insurance Corporation (FCIC), to renegotiate the agreement effective for the 2011 crop year. Due to significant increases in commodity prices in recent years, annual insurance industry payments more than doubled from $1.8 billion in 2006 to an estimated $3.8 billion in 2009. At the same time, the number of policies decreased. USDA says it has worked aggressively through the negotiation process to preserve the crop insurance program as part of the farm safety net, support producer access to critical risk management tools, protect the interests of taxpayers, and ensure a reasonable return for the companies that deliver the program.

As with the first draft of the SRA, USDA officials say the second draft provides companies with relatively stable administration and overhead subsidies per policy for seven major commodities and "will facilitate insurance company planning." RMA responded to some of the companies' concerns by adopting several modifications. For example, the second draft includes a transition period for companies to adjust to the new subsidy structure, an inflation factor for the subsidies after the transition period, and an additional 5 percent for subsidies "for operations in lower served states" which means states other than the Midwest's corn and soybean states.

The second draft of RMA's proposed risk-sharing terms represents RMA's efforts to "rebalance expected returns across the country" and to "more effectively reach under-served producers, commodities, and areas." In response to company concerns, RMA reduced the number of state groups from four to three and has modified the risk sharing terms for all states from the first draft.

This second draft of the SRA reflects USDA's six stated objectives for the agreement:

- ✓ Maintain producer access to critical risk management tools;
- ✓ Align Administrative and Operating (A&O) subsidy to insurance companies closer to actual delivery costs;
- ✓ Provide a reasonable rate of return to insurance companies;
- ✓ Protect producers from higher costs while equalizing reinsurance performance across states to more effectively reach under-served producers, commodities and areas;
- ✓ Simplify provisions to make the SRA more understandable and transparent; and
- ✓ Enhance program integrity.

In preparation for the ongoing negotiations with insurance companies, RMA contracted with an internationally known company, Milliman Inc., to review historical rates of return and determine a reasonable rate of return for the crop insurance industry. The full report is available at www.rma.usda.gov/news/2009/09/milliman.html.

For additional information on RMA's proposals for the new SRA go to: www.rma.usda.gov/news/2009/12/sra.html.

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