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In Most Years, Farmers Write "Big" Crop Insurance Checks[1]

Lost in all of the screaming headlines of the national press by crop insurance critics is the fact that in most years, farmers write premiums checks. The crop insurance critics forget, omit, misstate, or don't understand the following:

1. There is no cash subsidy transfer to a farmer unless there is a claim; otherwise a farmer writes a premium check.
2. Crop insurance is a premium cost-share program rather than a traditional subsidy that pays farmers cash. In most years, farmers write premium checks and do not collect an indemnity.
3. There are states where the farmer-paid premiums have exceeded the claims over the past 20 years, i.e. farmers in those states have netted none of the cash premium subsidy.
4. That does not mean that those states are over-rated, because one catastrophic loss year would wipe out all of the gains from the prior 20 years.
5. All of the catastrophic loss years with state loss ratios over 3.00 are in the Corn Belt, not the Great Plains (Table 1).
6. The U.S. Government Accountability Office (GAO), Risk Management Agency (RMA), etc. don't count the years with RMA underwriting gains, but they do count the loss years. The net taxpayer costs are equal to the "subsidy" plus the RMA underwriting gain or RMA underwriting loss. For example, in 2009, the subsidy was $5.427B and that is reported as the taxpayer "cost" for crop insurance by all of the government agencies, including GAO. However, the net payer cost is the

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$5.427B less the RMA gains of $1.435B for a net taxpayer cost of $3.992B, i.e. RMA underspent their budget, but credit is never given. In a loss year like 2012, there were $17.401B in claims, paid by $4.135B in farmer-paid premiums, $6.975B in subsidies, AIP's, which paid $1.313B in underwriting losses, and RMA, which paid $4.977B in underwriting losses. Thus, the net taxpayer cost for the 2012 year was $11.952B ($4.977B in RMA underwriting losses plus $6.975B in subsidies). However, 2012 was the worst loss ratio since 1993.

7. The average annual net taxpayer cost over the life of the ARPA Law (12 years) was about $4.1B; with A&O expense included the total cost was about $5.3B per year. The current Standard Reinsurance Agreement (SRA) caps the A&0 expenses to about $1.3B annually. There would also be cost for RMA employees and the administration of the program by the Secretary's Office.
8. The crop insurance program provides over $116B of coverage that provides the collateral for farmers to obtain reasonable financing that is necessary for a commercial-size efficient farmer to meet the market demands of a low cost producer. There is only about a dime's worth of wheat in a $3 loaf of bread at the supermarket! Only efficient commercial size farms can provide bread with 10 cents worth of wheat.
9. The current SRA allows RMA to retain a larger share of the underwriting gain and pay a smaller share of any underwriting loss. Had the current SRA been in place for the years prior to 2011, the RMA would have retained a larger share of the gain and paid a smaller share of the loss, especially in the Group 1 states.
10. Elimination of the large farms will shrink the size of the insurance pool. A larger insurance pool size spreads the risk over more farms, but if the pool shrinks as a result of public policy, then the national loss ratio may turn negative, requiring rate increases on the smaller farmers remaining in the insurance pool.
11. All of the current proposed changes including the limit on AGI would allow mega-sized farmers to change to CAT coverage with a 100% premium subsidy that requires no farmer paid premiums. They do pay a "small" processing fee.
12. A return to a government employee administered disaster program would provide the best protection to high-risk farming states. Because of farmer-paid premium costs, on average, Kansas farmers buy coverage that is 13 points lower than purchased in Iowa and Kansas farmers pay premium rates for that reduced coverage that are double those rates paid by Iowa farmers.
13. A payment limit on a direct payment that is paid every year is very different than the impact of a payment limit on crop insurance/disaster aid program. In most years, farmers don't have a claim and must write premium checks, but in the 1 year out of 10 years (varies by luck and region) when a loss occurs, an insurance payment that is capped will not cover a significant part of the loss for a commercial size farm. When new combines cost over $400,000 plus the header, then a $40,000 payment limit makes no sense as a risk management tool. If crop insurance is not going to provide a safety net for commercial agriculture, then why the need to provide a safety net for small part-time "hobby" farmers?

There are methods for reducing taxpayer cost for crop insurance that would not significantly harm agriculture. However, much of the debate seems to be based on two

positions; (1) the political left wants the safety net to return to a government employee run disaster program for “small” farms only; and (2) the political right wants the farm safety net eliminated. If the debate were simply over the cost-share of the premium farmers should pay versus taxpayers, then a reasonable compromise could be reached.

Few people are now arguing that crop insurance does not work. With the introduction of revenue insurance it targets payment to farmers who suffer financial losses rather than production losses. Under the price protection programs, when farmers had large yields it often causes prices to decline so farmers were collecting payments and with a big crop. When the crop failed, often times the price increased, but farmers had nothing to sell at the higher price.

Revenue Protection (RP) paid farmers in Iowa for 2012 revenue losses. Without the RP, Iowa growers would have had smaller claim checks or even no payments for the worst disaster since 1993. As in prior disaster years before the introduction of replacement-revenue crop insurance, there would have been calls for disaster payments in the middle of a Presidential election year. In the past, there were ad hoc disaster programs in nearly every year. After 30 years of RMA working to build a better crop insurance contract to prevent Congress from providing ad hoc disaster aid, now that crop insurance does work, many Congressmen want to eliminate the coverage.

The other nonsense argument is that if the government provided no crop insurance support, the private sector would provide the coverage. The real problem with crop insurance is the catastrophic loss year and how to rate for that year. In most lines of private property-casualty lines of insurance, about 65% of the premium is paid in claims, and varies little from year to year. However, on Minnesota corn RMA/AIPs have paid from 11% to a high of 827% of the premium in annual claims over the past 21 years. Loading a private rate to cover a potential 827% of premium claim year will generate rates higher than most farmers would pay. As a result it is likely most farmers would “self-insure” and just wait for the ad hoc Federal Disaster program based on their experience over the past 30 years. However, under ad hoc disaster aid, it is unlikely that regulators would allow ag banks and Farm Credit to use it as collateral. Under a premium cost share program, the crop insurance coverage provides over $100B of coverage to repay loans and cover lost expenses.

Would crop insurance ever payout $150B (coverage increase when harvest price increases) in claims? If it did, it would require nearly all of the USA insured acres to generate a zero yield. The problem would be no bread on the shelf in the super market and hungry people everywhere, i.e. a famine, something the USA has never seen.

The extremes in the loss ratios, caused by the correlation in crop losses, is the reason the stop-loss is needed in the SRA. To have crop insurance widely available and at affordable rates, it requires the catastrophic stop-loss protection from the government. The catastrophic stop-loss is the justification for government to be involved, and without that stop-loss protection, it is unlikely that large numbers of farmers would be able to buy coverage for perils like drought.

Table 1. All Crop Loss Ratios by State by Year

Yr	NE	IL	IN	IA	MN	KS	TX	MI	OK	MS	OH
2012	2.32	4.53	3.15	2.23	.30	1.70	1.31	1.21	.83	.42	1.25
2011	.35	.44	.58	.29	.53	1.36	2.36	.28	2.15	1.00	.41
2010	.34	.58	.35	.59	.15	.26	.38	.41	.33	.93	.24
2009	.28	.30	.25	.23	.24	.40	1.36	.61	1.65	1.24	.18
2008	.61	.66	1.17	1.20	.82	.62	1.27	1.01	.65	.76	1.76
2007	.19	.21	.37	.15	.45	.90	.38	.62	1.80	.66	.35
2006	.44	.10	.18	.16	.27	1.20	1.55	.28	2.18	1.08	.21
2005	.32	.77	.24	.23	.47	.45	.54	.27	.45	.45	.46
2004	.51	.38	.58	.31	1.03	1.16	.53	1.15	.53	.60	.77
2003	.79	.65	.89	.94	.61	1.34	1.36	1.05	.64	.87	.79
2002	2.01	.82	1.39	.25	.54	2.64	1.21	.74	1.73	.97	3.00
2001	.40	.26	.17	.66	.91	.95	1.53	1.55	1.53	1.79	.54
2000	1.32	.32	.37	.45	.44	1.38	1.80	.78	1.50	1.99	.54
1999	.43	.42	.84	.36	.67	.62	1.25	.36	1.71	1.20	1.26
1998	.34	.46	.86	.55	.36	.31	2.03	.62	.81	.83	.44
1997	.40	.23	.71	.10	.45	.21	.61	.33	.59	.38	.45
1996	.48	.61	1.07	.31	.26	1.58	1.65	1.35	2.42	.26	1.49
1995	1.05	.69	.91	.80	.60	1.09	1.26	.25	1.84	.99	.75
1994	.42	.12	.21	.07	.90	.33	.77	1.27	1.59	.79	.28
1993	1.88	.63	.55	4.65	6.10	1.40	.91	.96	2.27	1.87	.91
1992	1.54	.37	.55	.19	.79	1.59	2.86	1.89	1.62	1.00	.69
MAX	2.32	4.53	3.15	4.65	6.10	2.64	2.86	1.89	2.42	1.99	3.00
Min	.19	.10	.17	.07	.15	.21	.38	.25	.33	.26	.18
Avg	.78	.64	.73	.70	.81	1.02	1.28	.81	1.37	.96	.80

Table 2. The 12 Year Average Cost of Crop Insurance Post 2000 ARPA Act

Year	Corn Strike Price	Net Acres	$ Cov-erage	Gross Prem	farm-er paid	Goss Indem-nity	loss ratio	Underwriting Gain/Loss Gross	AIP	RMA	"Sub-sidy"	Net RMA	A&O[1]
		(000 000)						(000 000)					
2001	$2.46	211	36,729	2,978	1,206	2,965	1.00	12	346	(334)	1,772	2,106	636
2002	$2.32	215	37,299	2,909	1,168	4,058	1.39	(1,149)	(48)	(1,101)	1,741	2,842	626
2003	$2.42	217	40,621	3,434	1,392	3,259	0.95	176	377	(201)	2,042	2,243	734
2004	$2.83	221	46,602	4,186	1,709	3,291	0.79	895	691	203	2,477	2,274	888
2005	$2.32	246	44,259	3,945	1,601	2,341	0.59	1,604	915	689	2,344	1,655	829
2006	$2.59	242	49,919	4,709	2,027	3,551	0.75	1,158	822	336	2,682	2,346	959
2007	$4.06	272	67,340	6,547	2,724	3,465	0.53	3,082	1,572	1,510	3,823	2,313	1,333
2008	$5.40	272	89,892	9,832	4,141	8,719	0.89	1,113	1,095	18	5,691	5,673	2,009
2009	$4.04	265	79,575	8,949	3,522	5,216	0.58	3,733	2,298	1,435	5,427	3,992	1,619
2010	$3.99	256	78,104	7,592	2,882	4,235	0.56	3,357	1,919	1,438	4,710	3,272	1,368
2011	$6.01	266	114,112	11,959	4,506	10,807	0.90	1,152	1,666	(514)	7,453	7,967	1,330
2012	$5.68	283	117,127	11,111	4,135	17,401	1.57	(6,290)	(1,313)	(4,977)	6,975	11,952	1,316

Average Net Government Cost for Crop Insurance over 12 Years..... **$4.053** billion

Average A&O Cost for Crop Insurance..... **$1.137** billion

Avg. Farmer Cost for Crop Insurance..... **$2.584** billion

Average Insurance Companies (AIPs) Gains..... **$862** million

Average Gross Indemnity Payments..... **$5.776** billion

[1]Source: United States Government Accountability Office, "Crop Insurance; Savings Would Result from Program Changes and Greater Use of Data Mining", GAO-12-256, a report to the Ranking Member, Permanent Subcommittee on Investigations, Committee on Homeland Security and Governmental Affairs, U.S. Senate, March 2012. The A&O costs were capped in the 2013 Standard Reinsurance Agreement (SRA) at about $1.3 billion; mostly paid to agents for commissions. The A&O cap reduced the A&O payment by about $800 to $900 million. There are about $77-80 million in RMA employee and government operating expenses, in addition to the other costs.