Revisiting the Essential Strengths of Crop Insurance

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According to the United States Department of Agriculture (USDA), Americans spend 13 percent of their household income on food, coming in third behind housing and transportation. Farmers and ranchers work hard to help provide for American households, doing their part to grow safe, affordable and abundant food for consumers. However, farmers cannot control natural disasters or the prices set for the commodities they grow. To combat these unexpected situations, farmers and ranchers turn to crop insurance to protect their business.

This article focuses on the essential strengths of crop insurance, those pieces that make it so valuable to farmers, taxpayers and Congress alike. There are many reasons why crop insurance has become the centerpiece of the farm safety net. Farmers like the flexibility it provides them to pick the level of coverage plus the type of policy they want. Congress appreciates it because it works and provides a stable rural economy. Taxpayers approve of it because they aren't on the hook for 100 percent of the money needed, should there be a disaster, such as a drought, flood or falling commodity prices.

Producers receive individualized risk management solutions

Crop insurance is specifically tailored to each individual policyholder, covering the expected yield and revenue risk of each individual farmer. The farmer selects the level of coverage he wants, based on the historic or projected yield of the farm. Different rules govern new land brought into rotation or covering "risky" land. In addition, the producer may also receive coverage for prevented planting, planting losses and lower quality yields.

According to beginning farmer, Cody Bornholdt, crop insurance is the best fit for his farm due to the individuality the program offers. "Multi-peril insurance is the best fit in my mind, as we are a two county farm. Therefore, we are able to adjust our coverage per county. Knowing the past history of rainfall and the lay of the land, we are able to make it best suit our needs."

Crop insurance is not a "one-size-fits all" program, which is typical of many Federal programs, including Agriculture Risk Coverage (ARC) and Price Loss Coverage (PLC). Crop insurance is very specialized and sold through private insurance agents who are certified and highly trained to understand the complexities of the policy and provide advice and guidance to farmers as they select the best option(s) for their farm.

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Producers can use crop insurance as collateral for loans

After a natural disaster or economic downfall strikes, a farmer or rancher is expected to get back up on their feet and keep their business going to feed a growing world population expected to be 9 billion people by 2050. While farm programs also help pay for unexpected disasters, their timeliness can be a little more uncertain. Agricultural bankers prefer the timeliness crop insurance offers, allowing farmers to use crop insurance as collateral for operating loans.

Klodette Stroh farms malt barley, wheat, varieties of dry edible beans, corn and hay, with her husband and two sons in Powell, Wyoming. Given the experience she has had with banks, loans and crop insurance, she added that, "Bankers like to know that if you lose everything, something will be coming back to them."

With crop insurance farmers can financially recover from natural disasters and volatile market fluctuations; pay their bankers, fertilizer suppliers, equipment providers and landlords; purchase their production inputs for the next season; and give them the confidence to make longer term investments that will increase their production efficiency. Without effective and affordable crop insurance, catastrophic production losses would sap the rural economy by setting in motion a series of harmful events: farm failures and consolidation, job losses, farm-related small business failures, financial stress on rural banks and reduced investment in U.S. agriculture. A financially healthy rural economy requires a financially healthy farm production sector.

Producers are involved in, and take responsibility, for risk management choices

By helping to stabilize financial returns in agriculture, crop insurance maintains and promotes farmer investment in production capacity, enables the production sector to rebound quickly after disaster, and allows farmers to pay credit obligations and other input expenses. With crop insurance, farmers are entering into a contract with private insurers. That gives them much more certainty during the critical time of planting than some *ad hoc* disaster assistance expectations that may or may not happen.

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While farmers and ranchers rely on crop insurance agents to provide them with information about all of the policies and options available to them, producers make the final decision. In order for an agent to do his or her job, both the farmer and the agent must sit down together to design a management plan. From there, the farmer pays a portion for the coverage—a total of $3.6 billion in 2015—follows the good farming practices guidelines given in the contract and collects an indemnity only if a natural disaster or economic hardship occurs.

According to crop insurance agent, Todd Snider, "These growers are contributing this money into the pool and they might go 10 years without a loss. The Midwest may have a loss and then two years later California specialty crop growers might suffer a loss or a drought."

Producers can use crop insurance to improve their pre-harvest marketing plans

The Revenue Protection (RP) policy enables farmers to purchase policies that indemnify their lost production at the higher of the price projected just before planting time or the price at harvest. Projected price is just an estimate of the final price, per se, and farmers pay additional premium for this type of price protection. RP pays an indemnity at "replacement value," similar to what is available for homeowners insurance. It enables the producer to acquire the lost production at its replacement cost.

If there is a natural disaster that results in a large drop in production of a commodity, the price of that commodity is likely to increase sharply. Without this, the farmer's loss would be indemnified at the lower price projected at the start of the season. Unfortunately, such an indemnity would place many of them in financial jeopardy. Many farmers enter a forward contract to sell a portion of their production before harvest. Usually these contracts pay the producer for the production they deliver after harvest based on harvest prices. If they lose the crop, they are still obligated to deliver under the contract. But since the crop is lost, the farmer has to buy the commodity at the harvest price and deliver it or financially settle the contract. The purpose of Revenue Protection is to provide the farmer with sufficient funds to settle the forward contract.

Craig Corbett, a malt and seed barley farmer from Soda Springs, Idaho, said that while he can protect himself against price fluctuations with marketing tools, "the one thing that we can't have is nothing to sell. If I don't have anything to market, then I'm done. So if you're a producer, crop insurance is where you get the most protection for your buck."

Producers receive crop insurance indemnities in the timeliest way

One of the reasons why farmers strongly support crop insurance is that it is sold, administered, serviced and delivered by private-sector companies and knowledgeable licensed agents who will work around the clock if needed. Crop insurance combines the affordability and universality of the public sector with the speed, efficiency and flexibility of the private sector. As an example, in 2011, farmers in Texas received $2.6 billion in indemnities due mostly to drought. Of this, more than $1.3 billion was paid by mid-September of that year. Another example is during the 2013 government shutdown. Claims were paid, policyholders were taken care of, and the companies continued to operate "business as usual."

Government-run programs of the past were notoriously slow in their ability to deliver payments to farmers, often taking as long as 18 months to two years after a disaster for help to finally arrive. Crop insurance, on the other hand, is a highly dynamic program, which is closely tailored to each farmer's operation and is successfully managed and delivered by the private sector. That is why farmers,

and farm groups made crop insurance one of their top priorities in the 2014 Farm Bill.

Just a few months after buying his first crop insurance policy, the Yazoo River spilled over its banks and most of John Michael Pillow's farm was underwater. Pillow said that when the flood was at its height, the adjuster was on his farm surveying the damage and assuring him that his losses would be covered so he could bounce back. "Needless to say, I would be doing something else other than what I love, and I would be repaying the bank for the $2.5 million I borrowed to plant the crop for the rest of my life," Pillow said.

Producers do not receive excessive payments

As stated in many of our Crop Insurance in America testimonials, farmers do not pray for natural disasters to strike, nor do they long for the day when they have to collect crop insurance payments. However, they do value the peace of mind crop insurance can provide during their times of need.

The structure of crop insurance is such that companies have dollars at risk on every policy and are thus financially incentivized to reduce fraudulent claims. The industry has extensive training and education efforts including a certified loss adjuster proficiency program in which all adjusters must participate.

Because program integrity is vital for continued public support, fighting fraud, waste and abuse is a key priority for the industry and USDA through the RMA and the Farm Service Agency (FSA). There are numerous monitoring, review, audit, and other oversight requirements in the Standard Reinsurance Agreement (SRA). The private-sector crop insurance industry and RMA have fought to minimize fraud and have implemented effective and unprecedented measures to deter and identify false claims. The program has been a pioneer in the use of data mining, conducting thousands of reviews of claims data to ensure a high level of program integrity.

Data mining is a major effort to ensure program accountability. RMA has partnered with the Center for Agribusiness Excellence (CAE) at Tarleton State University, Stephenville, Texas, which has stored all of RMA's crop insurance data since 1996. CAE manages a centralized data warehouse, which is used to search, or mine, all data records to compare policies and detect individual producers whose policies demonstrate atypical patterns and to uncover broader patterns that may indicate potential waste, fraud or abuse. Through data mining, RMA annually develops a list of agricultural producers whose operations warrant an onsite inspection. This "spot check" list has proven to be an effective technique for deterring dishonest activity.

USDA's Office of Inspector General (OIG) provides another line of oversight by conducting audits designed to reduce vulnerabilities, strengthen integrity and provide RMA with oversight to help achieve efficient and effective program delivery.

Ultimately, Congress determines the role of government in crop insurance and relies not only on the above sources of information but also calls upon the Government Accountability Office and the Congressional Research Service to conduct reviews of crop insurance. Both entities issue periodic reports on their findings. Congress also conducts public oversight hearings to monitor the expenditure of public funds on crop insurance. These multiple layers of oversight provide a high level of confidence that the public funds used to support crop insurance are being properly spent.

Matthew King, a farmer from Delaware County, Ohio explains the frustration from hearing what the critics said. "It's so aggravating that during the 2012 drought, some outside groups opposed to farm policy charged that 'farmers were praying for drought, not praying for rain,' implying that we'd rather collect an indemnity check than get a decent harvest," King said. "Let me set the record straight on that one: I would take a better crop than a crop insurance payment every time, because well-marketed grain can make me far more money than any crop insurance indemnity ever would."

Producer indemnities are not capped by arbitrary payment limits

Crop insurance premium support is not biased against any farmer and remains size neutral. The industry also does not discriminate against specific incomes because we understand each farmer, no matter how little or big their farm is, produces food and materials needed to support our ever-growing population. When the unforeseen happens, the crop insurance industry wants all farmers to sleep easier at night knowing they will be able to plant again the following season.

Reducing financial risk helps a farmer maintain, expand, and increase the efficiency of the farm, improves access to credit, increases investment in production assets and enables the farm to recover after disaster. These are benefits to farmers, both large and small, and to our society as a whole.

The 2014 Farm Bill took steps to make crop insurance even more attractive to small farms, including organic operations and those run by new and beginning farmers.

It should be noted that every acre enrolled in crop insurance helps spread risk, which ultimately lowers premiums for all. Therefore, the involvement of larger, more efficient operations, helps bring down costs for smaller farms and keeps crop insurance affordable.

By reducing financial risks and facilitating investment, crop insurance may contribute to increasing farm size, but analysts have estimated the impact is quite small and dominated. Over the years a higher and more diverse participation, combined with better data, improved the program's actuarial performance by reducing adverse selection and enhancing underwriting and ratemaking. Reduced participation would also only lead to an increase in calls for off-budget, *ad hoc* disaster programs that have been largely averted since the Federal crop insurance program was modernized in 2000.

To further prove our point, USDA has even called a cap on premium support "ill advised," noting regions with high value crops, large-acreage farms, and/or a higher risk of crop loss would be especially hard hit. A dramatic increase in premium costs on a large percentage of acres would inevitably lead to decreased participation in the crop insurance program.

Former economic adviser to the crop insurance industry, Dr. Keith Collins shared his take on the evolution of the program throughout history. "Look at the (crop insurance) program that we have today, look at where it came from, look at how it evolved, how it emerged as the best of many different programs that were tried over the years," Collins said. "And the success of the program has hinged on it being available to producers widely across America, being affordable for producers large and small, and having a private-sector [component] that is financially viable."

Producers share in the program cost

In order to participate in the crop insurance program, producers must put "skin in the game." Though crop insurance is partially subsidized by the Federal government, the money farmers put towards the program helps defray taxpayer costs and encourages financial discipline.

Losses are shared by farmers, private-sector crop insurance companies and the government. For example, following the 2012 drought, farmers received $17 billion in indemnity payments to cover losses after paying approximately $4.1 billion in premiums and shouldering deductibles of approximately $12.7 billion. Private insurers had a $1.3 billion underwriting loss in 2012 because premiums did not offset claims. The government fulfilled its contractual obligation in the SRA as a reinsurer and provided premium support to farmers.

This stands in sharp contrast to *ad hoc* disaster bills, which are funded entirely by taxpayers and were needed to offset farmer losses prior to the emergence of modern-day crop insurance. Forty-two such emergency disaster bills in agriculture have cost taxpayers $70 billion since 1989, according to the Congressional Research Service.

Danny Davis, a cotton farmer in Elk City, Oklahoma, has purchased crop insurance every year since the early 1990s. The first time he used it was during an August hailstorm in 1996. "We lost all but about 200 acres of our cotton," Davis said. "There is no doubt in my mind that hail storm would have been the end of our farming operation had it not been for crop insurance."

Producers benefit from the efficiencies and service of the private sector delivery system

Most would agree that the private sector excels at some tasks while the government is better-suited for others. This melding of the private and public sectors has yielded a crop insurance policy with affordable premiums, personalized risk management solutions and a private delivery system that puts needed monies into the hands of farmers when timing is critical.

Crop insurance covers 128 crops, including all major grain crops and cotton, nursery, citrus, rice, potatoes, and livestock. Farmers can cover their crops for all natural disasters, including wildfire, earthquake, volcanic eruptions and even irrigated water issues. Because the policy is personalized, each farmer tailors the policy to match his specific risk and desired coverage.

Corn and soybean farmer Quentin Bowen, who operates a family-farm in Humboldt, Nebraska, says that when disaster strikes, the difference in delivery of benefits when comparing government-run programs to the private sector's handling of crop insurance, is like comparing night to day. "The speed of delivery of crop insurance—because it's administered by private sector companies—makes it a different kind of animal. In fact, if a natural disaster strikes and I'm covered by a crop insurance policy, typically the payment comes to me in one or two weeks, not in one or two years."

Currently, there are 17 private-sector companies devoted to delivering crop insurance to farmers that best fits their needs. The companies employ more than 20,000 licensed agents, certified loss adjusters and company staff. Furthermore, companies invest heavily in technology, infrastructure efficiency, training programs and service improvements for farmers and ranchers.

Beyond fulfilling their delivery and service obligations, insurers have contributed to improving the program by providing input and feedback on the implementation of ever-changing rules and policies. Farmers benefit from private-sector efficiency, which speeds payments when needed most, and taxpayers benefit from reduced overhead costs and strict procedures to combat waste, fraud and abuse.

Steven Rutledge, Farmers Mutual Hail Insurance Co. of Iowa said during his 2012 Congressional testimony that, "We firmly believe that crop insurance should remain the core risk management tool, and we are committed to the public-private partnership of program delivery, which directly supports more than 20,000 private sector jobs across the country. The private sector should continue to provide and deliver crop insurance options, share in the risk of loss caused by changing markets and natural disasters, and adjust losses for insurable crops. We believe the private sector, not the government, is the best way to provide the individual risk management information and tools that are indispensable for producers today. We understand that is the way farmers and ranchers want the program to operate, and trust in our congressional leaders to stay the course."

Crop insurance is comprehensive and program features can be adjusted quickly

The Federal government and private crop insurance companies understand that there is not a one-size-fits-all insurance program for producers across the United States. Taking into account different environmental and crop demands, crop insurance program features can be adjusted to cover an individual's farm quickly and efficiently. Having the flexibility to make major program adjustments also imposes financial discipline on the government because it has the authority to correct or eliminate programs and features that are not working.

In its formative years, crop insurance was available for only a handful of commodities. For example, in 1948, insurance was only available for wheat, cotton, flax, corn and tobacco for a total of 391 county-crop programs, a fraction of what is available today. Today, crop insurance is available for more than 120 commodities and has more than 62,000 county-crop programs and premium support rates are the same across commodities for each plan of insurance.

Expansion to additional crops and new provisions and plans of insurance have been the result of Congressional actions, notably in farm bills; RMA contracting with private entities often at the request of farmers; and new pilot programs introduced through the 508(h) process, also spurred by producer interest. The Federal Crop Insurance Corporation (FCIC) Board of Directors must approve new pilot programs before they are made available to farmers and then field tested for three or more years, which is a time consuming process. Through these means, crop insurance has been successfully expanded to many new specialty crops in recent years as well as to pasture, range, forage and livestock products. New insurance plans, such as Actual Revenue History and Whole Farm Revenue Protection, have been designed to improve coverage for specialty crop and diversified farmers. The result of these ongoing efforts has been an increase in affordable financial protection for many farm types across the country.

The 2014 Farm Bill alone provided agriculture with Supplemental Coverage Option (SCO), a standalone insurance policy for cotton (STAX), provisions for beginning farmers that will help increase assistance, and an expansion of crop insurance for organic growers.

Stanley Wilson, a cotton, carrot, potato and raisin grape farmer from Shafter, California, explained crop insurance supplies comprehensive coverage to producers who endure various farm disasters. "Anyone who's been in farming knows that production is not consistent. Many times we have problems caused by climate, insects or diseases and we need protection against those things to control a complete wipeout."

Crop insurance has already contributed to deficit reduction

Throughout history, crop insurance has helped reduce the United States' budget deficit and it continues to help save taxpayers millions of dollars each year. Looking back, the 2014 Farm Bill projected crop insurance would save $24 billion. In 2011, $4 billion of the overall $6 billion reduction from SRA renegotiations between the Federal government and private insurance companies went directly towards deficit reduction. With the 2008 Farm Bill, $6.4 billion was cut from the crop insurance industry, contributing to deficit reduction as well.

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Absent crop insurance, the cost of natural disasters that cripple America's farmers would fall directly on the laps of taxpayers, which happened repeatedly before the widespread use and availability of crop insurance.

The 2014 Farm Bill cemented crop insurance as the cornerstone of farm policy. Under this policy, farmers shoulder a portion of the risk along with private-sector crop insurance companies. Unlike the past, farmers must first purchase crop insurance—putting "skin in the game"—before being protected, and must shoulder a portion of the losses through deductibles. This ensures that farmers are active participants in risk management and that taxpayers are not being asked to bear all the burden of natural disasters in farming.

National Crop Insurance Services' President, Tom Zacharias, says "the crop insurance industry shares the belief that deficit reduction is important. In fact, crop insurers have contributed more than most other industries to the goal of deficit reduction in recent years."

Crop insurance has flexibility to help meet World Trade Organization disciplines

The World Trade Organization (WTO) is an international organization that helps:

- Settle disputes and reduce trade tensions
- Stimulate economic growth and employment
- Encourage good governance
- Help countries develop

To help ensure each of these goals are achieved, the WTO has defined limits to certain levels of domestic support. These levels are amber, red, blue and green. According to WTO's chart, "green" means the subject is permitted, "amber" means the subject should be reduced, "red" means it is prohibited and "blue" is for subsidies that "are tied to programs that limit production."

"Crop insurance is critically important," said Dan Kidd, a farmer from Big Sandy, Montana. "Our competing countries have different mechanisms that they utilize that are under the 'green box'. And that's allowed, just like the disaster program. Crop insurance falls into what they call the 'de minimis' level and portions of the subsidy falls into the de minimis amber."

Conclusion

Farmers and ranchers work hard every day to provide food and materials to American consumers and global markets. Each crop insurance essential strength can be seen as a beneficial part of helping provide America and global markets with the resources they need. Crop insurance was established under the Federal Government in 1938 and throughout the years it has evolved and adapted to the needs of our farmers. Crop insurance helps safeguard a farmer's crop and business as a whole and without it, our food source may not be as plentiful or affordable as it is today.

Secretary of Agriculture, Tom Vilsack summed up the importance of crop insurance best when he said, "In the wake of a devastating disaster, crop insurance offers a lifeline. It is one of the most important, reliable and cost-effective parts of the safety net here in the United States."