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2014 Farm Bill: Crop Insurance Changes

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Disclaimer

1. Analysis is based on my reading of Managers Report and the Law. It also includes my crop insurance experience and communications with Washington decision makers. There is not a "one size fits all" program and farmers will have to make financial decisions that carry risk of a financial loss or gain. This analysis carries no warranty given or implied by Kansas State University or the author.

2. Many of the results will not be known until USDA publishes the implementation regulations for the new farm programs. Signup is unlikely until this fall.

Crop Insurance Changes

1. 60% yield plug for replacing low yields in an APH was retained.
2. If a county has a 50% yield loss, then farmers may drop that year's yield from their APH. The APH will be 9 years of yields divided by 9. If the county yield trigger is met more than once, then more than 1 yield may be excluded.
3. Conservation compliance required to receive crop insurance premium subsidy, but farmers are given time to fix compliance problems.
4. Out-of-compliance farmers may buy crop insurance, but without subsidy.
5. May out-of-compliance farmers elect CAT that only has an implied premium and pay only a $300 fee?

Crop Insurance Changes

1. A 10% increase in crop insurance premium subsidies for beginning farmers.
2. Crop agents are allowed to correct errors.
3. All farmers in conservation compliance and not participating in ARC or STAX may purchase SCO.
4. SCO covers planted acres and if the above conditions are met, SCO can be purchased on crop land that has no base in addition to base acres.
5. Because we are past the crop insurance contract change date, all crop insurance changes will start with the 2015 crop. One would assume this means the winter wheat crop will be the first crop to implement the crop insurance changes.

SCO Not Defined

1. USDA has an "understanding" with the Ag Committee that RMA will follow the Area Risk Protection Insurance (ARPI was GRIP) rating and underwriting method.
2. SCO sold via crop insurance agents and AIP insurance companies.
3. A&O capped at 12% and outside the $1.3 Billion A&O limit.
4. ARPI has no stop loss and farmers can buy 120% times the expected value of the crop. SCO is limited to 100% of the crop value and liability is tied to the farmer's crop insurance deductible.
5. No SCO for crops in ARC or STAX.
6. SCO starts in the 2015 crop year; PLC & ARC in 2014.

Supplemental Coverage Option (SCO)

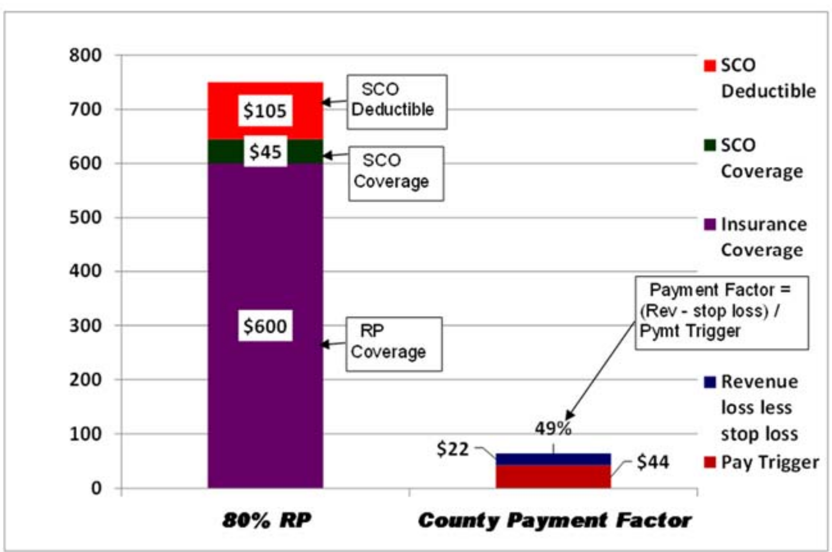
Guarantee	County Revenue
Reference Price	Crop Insurance Prices Based on Futures
SCO Liability covers RP, RP-HPE, or YP Deductible up to 86%	Farmer's APH X Crop insurance Prices X (86%-% CI Coverage), determined by type of coverage purchased
SCO Payment Trigger	86% X Expected County revenue
Actual County Revenue	County Yield X Harvest Price
County % Loss	Actual County Revenue / 86% Expected County Revenue adjusted for % CI stop loss
Farmer Payment	% County loss X Farmer's Liability
Payment Acres	Covers all Planted Acres
YP base Coverage	86%-% Coverage of Farmer's CI policy
RP-HPE base Coverage	86%-% Coverage of Farmer's CI policy
RP base Coverage	86%-% Coverage of Farmer's CI policy
Payment Limit	None & No Sequestered Payments
Max Payment per AC	Stop Loss @ % Crop Coverage Level
Program Selection	1 time Select ARC or PLC + SCO

Example Farmer Values for Supplemental Coverage Option's (SCO)

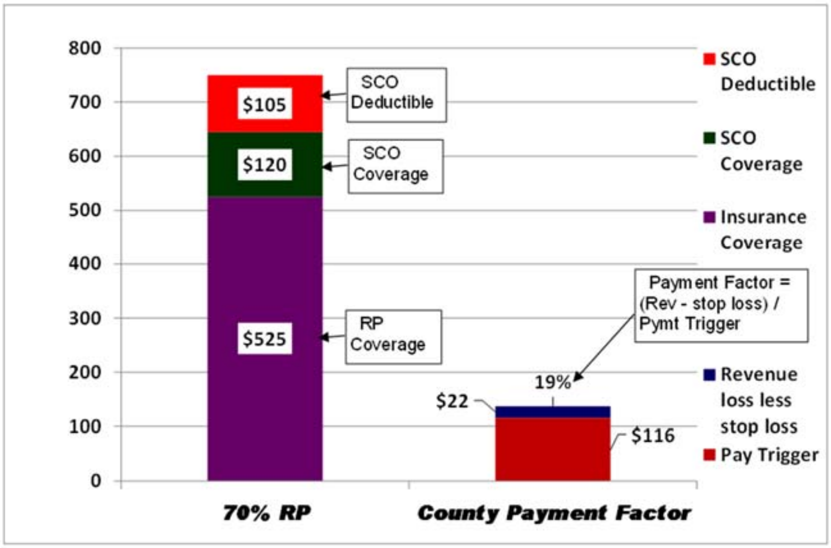
	Farm	County
APH	150.0	145.0
Base Price	$5.00	$5.00
Total Revenue	$750.00	$725.00
Harvest Price	$4.30	$4.30
Final Revenue	$750.00	
% Coverage	70%	70%
RP Guarantee	$525.00	
Final RP Guarantee	$525.00	
Harvest Yield	135.0	140.0
Revenue to Count	580.50	602.00
RP Payment	0.00	
Payment Factor*		19%
Protection Factor	100%	
SCO Coverage	120.00	
SCO Payment	22.24	
Total Payment	22.24	

*Payment Factor was calculated based on Area Risk Protection Insurance (ARPI) payment factor. RMA may use some other method.

Supplemental Coverage Option's (SCO) Liability is tied to the Deductible in 80% RP



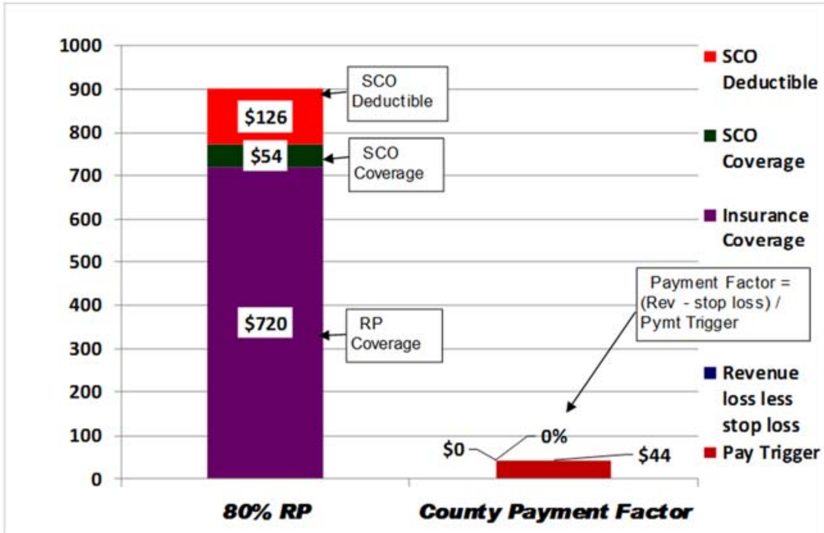
Supplemental Coverage Option's (SCO) Liability is tied to the Deductible in 70% RP



SCO Payment Trigger Include Harvest Price?

1. "100% coverage limit" might be interpreted as expected county yield times the base crop insurance price. Therefore, higher harvest prices would reduce or eliminate the SCO county payment trigger.
2. The SCO dollars of liability would increase for the RP insured farmers, if the harvest price is greater than the base price.
3. If the harvest price adjustment is not used in the SCO county trigger, similar to the APRI payment trigger that includes the harvest price, SCO payments will be cut even with a larger dollar amount of liability.
4. In the example farm if the harvest price increases to $6 and a county's actual yield equals 110 bu., then the SCO coverage increases from $45 to $54, but the county trigger would equal zero, unless the harvest is included in county trigger. As result there is no SCO payment.

Impact on SCO from a $5 MP Price Increase to a $6 Harvest Price



SCO Payments Based on Example Farm Scenarios

1. 80% RP & SCO, price declines from $5.00 to $4.30 and a 140 bu. actual county yield
   49% County Trigger X $45 SCO Liability = $22.24 SCO payment
2. 70% RP & SCO, price declines from $5.00 to $4.30 and a 140 bu. actual county yield
   19% County Trigger X $45 SCO Liability = $22.24 SCO payment
3. 80% RP & SCO, price increases from $5.00 to $6.00 and a 110 bu. actual county yield
   0% County Trigger X $54 SCO Liability = $0.00 SCO payment

SCO Corn Premium Cost Estimate for the Corn Belt; A SWAG?

RP Guarantee 80% Converge	$600.00
RP Rate	6.9%
Premium per acre	41.66
Farmer Paid Premium/ ac	$13.33
SCO Coverage	$45.00
Rate	31.6%
Gross premium	$14.22
Farmer Paid SCO Premium*	$4.98

*Adding harvest price to the SCO payment trigger would increase the premium by about 40% to 50%. The estimated SCO non-subsidized premium rate with a 70% stop loss (70% RP) would be about 17.7%. The gross premium rate at this location was 6.9% for 80% RP and 4.4% for 85% APRI-HPE.

Where Does SCO Fit?

1. Some counties don't have coverage offers greater than 75%.
2. Farmers with significantly more crop acres than base acres.
3. Counties with very high rates for 80% and 85% RP coverage.
4. If the county trigger is not adjusted for higher harvest prices, then SCO will be a less attractive buy for RP insured farmers.
5. An 80% Enterprise unit has a greater subsidy than SCO.
6. Risk averse corn-soybean farmers who are willing to forego a "likely small" ARC payment because they want to avoid a catastrophic price collapse by selecting PLC & SCO over ARC.

Defining County Yield is Critical

1. Planted acres?
2. Harvested acres?
3. Harvested acres plus failed acres? Will failed acres include prevented planted acres?
4. RMA has the T-yield that is a county yield based on planted acres.
5. Trend adjusted expected county yield?
6. Other definitions for county yield

Defining County Yield is Critical

1. NASS has many missing county values, so likely RMA data will need to be used to fill in missing data.
2. The county yield used for the 50% county trigger to allow a yield to be excluded from an APH is a simple average county yield.
3. The ARC county yield is an Olympic average yield.
4. One would assume the same ARPI county yields would be used for SCO. However, this only sets the payment trigger, the SCO payment is based on the individual farmer's deductible in their crop insurance coverage.

SCO Not Defined

1. Farmers have a basis risk in SCO, because farmers can suffer a loss and not have the county meet the payment trigger, so no payment. If the county trigger has been met, then the payment is the county percent loss times the Farm level deductible below 86% and above the crop insurance percent coverage.
2. SCO will pay claims about 6 months before PLC and ARC payments are made because those payments must wait on the national marketing year average price to be finished.
3. SCO payments cannot be sequestered, no payment limits, large farms will have less basis risk, based on crop insurance prices, cover all planted acres, it is an annual decision to buy, the amount and type of coverage is also an annual decision.
4. Farmers must pay 35% of the premium.

FAPRI Estimates of Commodity Program Participation

Crop	PLC	ARC-county	ARC-Farm	SCO**	STAX**
Corn	50.00%	37.50%	12.50%	25.00%	n.a.
Soybeans	40.00%	45.00%	15.00%	20.00%	n.a.
Wheat	70.00%	22.50%	7.50%	35.00%	n.a.
Cotton	n.a.	n.a.	n.a.	0.00%	95.00%
Sorghum	80.00%	15.00%	5.00%	40.00%	n.a.
Barley	90.00%	7.50%	2.50%	45.00%	n.a.
Rice	90.00%	7.50%	2.50%	45.00%	n.a.
Peanuts	90.00%	7.50%	2.50%	45.00%	n.a.

*PLC and ARC are percent of base acres. SCO and STAX are percent of planted acres.
**SCO and STAX are not available until 2015

When will Farmers Need to Make a Final Decision on Farm Program Participation

1. Secretary Vilsack's addresses to Commodity Classic on Farm Bill implementation February 28, 2014 - San Antonio, Texas

   "We will allow you during the course of that summer and fall to update production history. We want to make sure we are communicating with you about base and yields in your production history. We are going to hope to publicize and focus on publicizing the final program and the regulations for both **ARC and PLC in the Fall of 2014**."

2. Their will be no payments until Fall of 2015 on the 2014 crop because of the wait for the completion of the MYA price.

3. Therefore, the longer it takes for signup, the better for Farmers, because the current price and yield forecasts will change from forecast to history and allow for a more informed decision.

More Analysis and Education

1. None of the crop insurance changes will be made unitl the 2015 crop because we are past the contract change date.

2. It is assumed that SCO will be available on the fall planted wheat crop that will be harvested in 2015.

3. Free signup for AgManager.info that covers crop and livestock marketing, government programs, crop insurance, leasing, farm management and public policy issues.

4. Please feel free to send comments or questions on this presentation to AgManager.info


Thank You
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