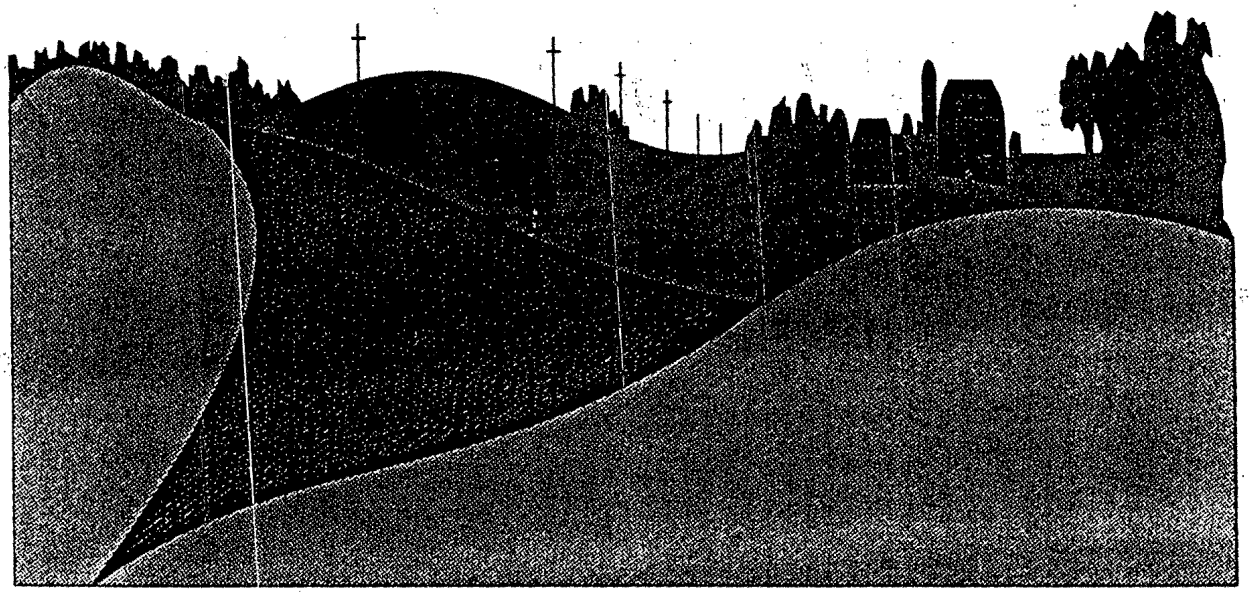
History of the U.S. Department of Agriculture 1993-2000
Archival Documents
Chapter 1: Farm Policy Risk Management Agency

Federal Crop Insurance Reform Act of 1994

Reform Guide
Reform Guide (Spanish)
Briefing Kit
1995 Report to Congress
1996 Report to Congress
Agricultural Communicators Kit
Press Release announcing passage
Fact Sheet
Manager's Bulletin's implementing FCIC Board of Directors
Crop Insurance Reform Congressional Briefing

REFORMING



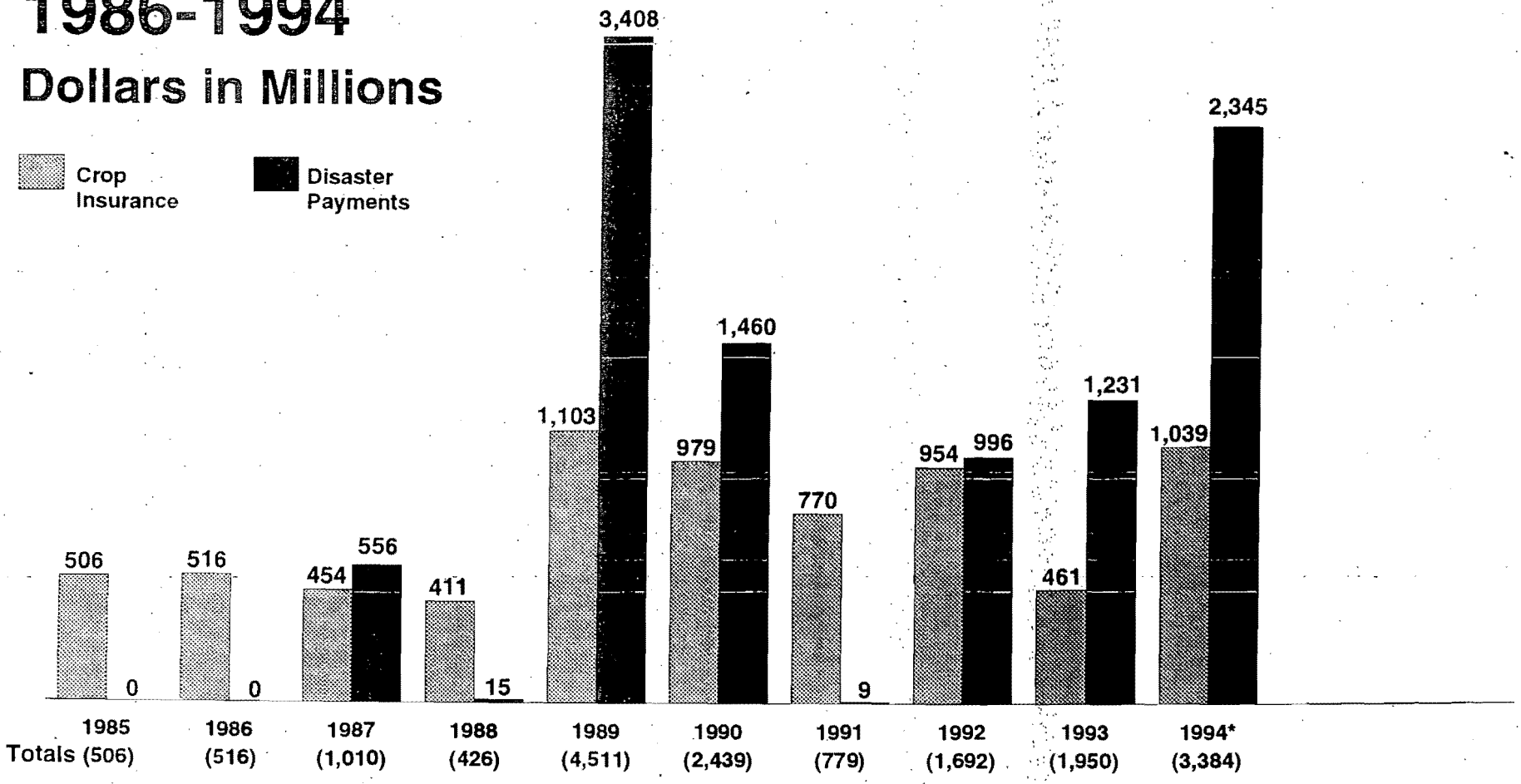
FEDERAL CROP INSURANCE

FCIC/USDA

1994

Federal Outlays for Crop Emergency Aid 1986-1994

Dollars in Millions



Crop Insurance, 6 Year Average (1989-94) 884-10 Year Average (1985-94) 719
Disaster Payments, 6 Year Average (1989-94) 1,575-10 Year Average (1985-94) 1,002

*Estimate

Market Value

UNITED STATES CROP VALUE SUMMARY

INSURED CROPS

NATIONAL VALUE OF ALL CROPS $92,385,311,215

CROP	REPORTED ACRES	DOLLAR VALUE	PERCENT OF TOTAL VALUE
Corn, Grain	66,950,480	18,008,691,703	19.493
Soybeans	56,498,545	11,213,520,994	12.138
Wheat	69,353,948	7,296,722,323	7.898
Cotton, Upland	11,501,930	4,884,989,171	5.288
Tobacco	732,740	2,829,953,119	3.063
Potatoes	1,363,816	2,396,315,957	2.594
Nursery, Container		2,375,462,434	2.571
Corn, Silage	6,124,202	1,954,333,349	2.115
Oranges	770,214	1,515,565,984	1.640
Apples	352,114	1,408,875,579	1.525
Peanuts	1,807,325	1,256,883,370	1.360
Sorghum, Grain	9,086,031	1,203,379,180	1.303
Sugar Beets	1,375,468	1,125,379,300	1.218
Rice	2,812,429	1,040,085,810	1.126
Tomatoes - Fresh	137,578	924,639,769	1.001
Barley	7,505,000	906,414,000	0.981
Grapes - Processed	408,090	885,062,003	0.958
Sugarcane	723,840	813,706,190	0.881
Raisins	266,737	677,942,810	0.734
Beans, Dry	2,099,403	660,075,798	0.714
Almonds	413,202	639,048,900	0.692
Tomatoes - Processed	353,911	617,956,960	0.669
Grapes, Table	90,343	494,035,398	0.535
Onions	146,180	493,421,041	0.534
Peaches	117,823	482,137,001	0.522
Oats	6,015,517	412,485,275	0.446
Grapefruit	168,928	354,979,543	0.384
Lemons	59,816	347,117,610	0.376
Pears	50,031	281,428,961	0.305
Plums - Fresh	45,199	265,029,699	0.287
Sweet Corn - Fresh	191,672	256,059,591	0.277
Walnuts, English	184,837	254,412,036	0.275
Sunflowers	1,854,495	247,439,110	0.268
Peppers	53,513	225,972,741	0.245

UNITED STATES CROP VALUE SUMMARY

INSURED CROPS

NATIONAL VALUE OF ALL CROPS $92,385,311,215

CROP	*REPORTED ACRES*	*DOLLAR VALUE*	*PERCENT OF TOTAL VALUE*
Sweet Corn - Processed	476,613	213,509,890	0.231
Nectarines	25,761	158,609,100	0.172
Cranberries	27,801	152,828,500	0.165
Beans, Snap - Processed	214,640	139,856,244	0.151
Prunes	79,707	133,203,850	0.144
Peas, Green	293,750	109,804,780	0.119
Tangerines	18,922	69,225,312	0.075
Apricots	20,249	48,509,599	0.053
Peas, Dry	274,500	43,363,600	0.047
Macadamia Nuts	18,700	41,720,000	0.045
Safflower	159,073	37,924,863	0.041
Flax	253,002	20,858,600	0.023
Tangelos	10,419	16,897,699	0.018
Figs	13,071	16,351,600	0.018
Beans, Lima - Processed	21,650	9,432,000	0.010
Temples	9,199	7,641,999	0.008
TOTAL		69,969,260,345	75.736

"Nursery, Container" crops are container grown landscape plants.

Values are not available for the following insured crops: Popcorn, Hybrid Seed Corn, Hybrid Seed Sorghum.

Acreage data is incomplete for apples, peaches, pears and plums.

CROP EXPANSION FEASIBILITY STUDY LIST

Feasibility studies are currently underway on the following crops in anticipation of developing new crop programs:

AVOCADOS
ASPARAGUS
BLUEBERRIES
BROCCOLI
CANOLA
CANTALOUPE
CARROTS
CAULIFLOWER
CELERY
CHERRIES-SWEET
HAY-ALL
HAY-HAYLAGE
HAY-OTHER
LETTUCE-HEAD
LETTUCE-LEAF
MUSHROOMS
NURSERY CROPS
PECANS
PEPPERMINT
PINEAPPLE
PISTACHIOS
SEED-FORAGE
SEED-LAWN
STRAWBERRIES
SWEET POTATOES
WATERMELON

TARGETED SUBSIDIES FOR BUY-UPS
COMPARISON OF FARMER'S OUT-OF-POCKET EXPENSE

WITH TARGETED SUBSIDY FOR BUY-UPS:

Coverage Level	Current Cost	Cost Under Reform Act	Difference
65% of yield	$296	$246	-17 percent
75% of yield	$623	$574	- 8 percent

WITHOUT TARGETED SUBSIDY FOR BUY-UPS:

Coverage Level	Current Cost	Cost Under Reform Act Without Buy-up Subsidy	Difference
65% of yield	$296	$282	- 5 percent
75% of yield	$623	$609	- 2 percent

Assumptions:

100 acres planted/ 100 bushel yield/ $1.00 price election
10 percent premium rate for 75 percent coverage

Stated costs are the farmer's out-of-pocket cost for the coverage after deducting the subsidy.

FEDERAL CROP INSURANCE CORPORATION
PREMIUM/INDEMNITIES/LOSS RATIOS
1981 – 1993 (Crop Year Data)
(dollars in thousands)

YEAR	PREMIUM	INDEMNITIES	LOSS RATIO
1981	$379,169	$408,101	1.08
1982	398,671	528,157	1.32
1983	291,353	587,691	2.02
1984	435,588	639,969	1.47
1985	439,733	684,364	1.56
1986	381,753	616,993	1.62
1987	366,640	369,163	1.01
1988	437,654	1,053,775	2.41
1989	820,763	1,215,763	1.48
1990	838,040	1,028,581	1.23
1991	737,146	953,257	1.29
1992	758,768	920,901	1.21
1993 (est.)	784,652	1,412,374	1.80
TOTAL 1981 – 1993	$7,069,930	$10,419,089	1.47
AVERAGE 1981–1993	$543,841	$801,468	1.47

1992 Figures – Actuals from Oct. 27, 1993 Summary of Business
1993 Figures from Damage Report of Oct. 20, 1993.

CORN - PARTICIPANT

Comparison between Disaster Assistance and MPCI proposed Catastrophic Coverage

DOES NOT INCLUDE DEFICIENCY PAYMENTS RECEIVED

Assumptions:

APH yield = 120 bushels
ASCS Yield = 100 bushels
MPCI price = $2.30/bu
ASCS target price = $2.75/bu
ASCS deficiency pymt = $0.45/bu
Acres planted = 90

	Farm	Per Acre
Disaster (.5004 pro-rate)	$3,952.00	$43.91
Disaster (No pro-rate)	$7,898.00	$87.76
Catastrophic Protection	$7,776.00	$86.40

FEDERAL CROP INSURANCE CORPORATION

CROP INSURANCE REFORM COMPARED TO DISASTER ASSISTANCE

CORN NON-PARTICIPANT

YIELD LOSS %	100% PRORATE	50% PRORATE	REFORM PLAN
	$ PER ACRE		
100	80	40	86
90	67	34	69
80	54	27	52
70	41	20	35
60	27	13	17
50	18	9	0
40	0	0	0

ASSUMPTIONS:

COUNTY AVERAGE YIELD	120	BUSHELS PER ACRE
DISASTER ASSIST. PAYMENT	$1.12	PER BUSHEL
APH YIELD (REFORM PLAN)	120	BUSHELS PER ACRE
PRICE ELECTION	$2.40	PER BUSHEL

FEDERAL CROP INSURANCE CORPORATION

CROP INSURANCE REFORM COMPARED TO DISASTER ASSISTANCE

SOYBEANS

YIELD LOSS %	100% PRORATE	50% PRORATE	REFORM PLAN
	$ PER ACRE		
100	100	53	80
90	88	44	64
80	71	36	48
70	53	27	32
60	35	18	16
50	18	9	0
40	0	0	0

ASSUMPTIONS:

COUNTY AVERAGE YIELD	45 BUSHELS PER ACRE
DISASTER ASSIST. PAYMENT	$3.91 PER BUSHEL
APH YIELD (REFORM PLAN)	45 BUSHELS PER ACRE
PRICE ELECTION	$5.90 PER BUSHEL

COTTON

Comparison between Disaster Assistance and MPCI proposed Catastrophic Coverage

EXAMPLE #1

Assumptions:

APH yield = 406 pounds
ASCS Yield = 406 pounds
MPCI price = $0.53/lb
ASCS target price = $0.729/lb
ASCS deficiency pymt = $0.186/lb
Acres planted = 92.5

	Farm	Per Acre
Disaster (.5004 pro-rate)	$3,813.00	$41.22
Catastrophic Protection	$5,971.25	$64.55
Disaster (No pro-rate)	$7,620.00	$82.38

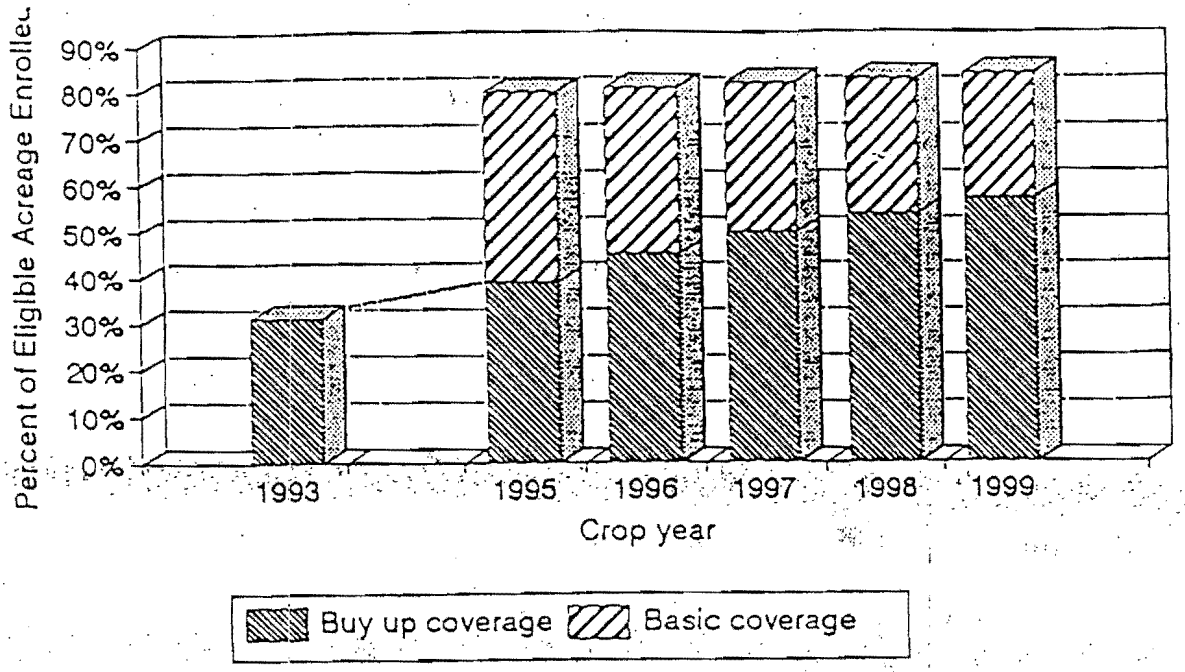
EXAMPLE #2

Assumptions:

APH yield = 383 pounds
ASCS Yield = 406 pounds
MPCI price = $0.53/lb
ASCS target price = $0.729/lb
ASCS deficiency pymt = $0.186/lb
Acres planted = 92.5

	Farm	Per Acre
Disaster (.5004 pro-rate)	$3,813.00	$41.22
Catastrophic Protection	$5,633.00	$60.90
Disaster (No pro-rate)	$7,620.00	$82.38

Participation Under the Reform Proposal
(with linkage)



- Under the reform proposal, producers who participate in price support and income support programs or who have loans under any program of the Farmers Home Administration are required to obtain at least the catastrophic level of insurance for *all crops of economic significance* farmed in the county in which that producer has an interest. The linkage with commodity programs will ensure that participation in the crop insurance program is 80 percent of eligible acreage in 1995.

- Requiring producers to obtain catastrophic crop insurance for *program crops only* would potentially lower the crop insurance participation rate as significant crops (e.g., soybeans) would be largely unaffected. Participation rates would likely be only as high as 65-70 percent of eligible acreage.

- If crop insurance is not linked to commodity program eligibility it is likely that crop insurance participation will be only 55-60 percent of eligible acreage, at least in the early years of program operation. Lower participation rates could encourage ad hoc disaster assistance which would further undermine participation.

Crop Emergency Aid
Projected Taxpayer Savings

Dollars in Millions

	Total 1995-99
Current Divided Approach:	
Crop Insurance:	3,900
Ad Hoc Disaster Relief:	5,000
Total Current	8,900
New Combined Program:	8,100
Taxpayer Savings:	$750*

Source: Budget of the United States Government Fiscal Year 1995
*Minimum Based on Rounding Off in Budget

FEDERAL CROP INSURANCE REFORM ACT OF 1994
Summary of Key Elements

1: **Repeal of ad hoc disaster authority:** Current legal authorities for ad hoc crop loss disaster relief are repealed. In the future, the program outlined below will replace these disaster bills as the Federal response to emergencies involving widespread crop loss.

As added protection, a parliamentary hurdle is erected: future ac hoc relief measures are placed on budget. The current Budget Act exemption for these bills is scaled back.

2: **Catastrophic crop insurance coverage**: The Federal crop insurance program is supplemented with a new catastrophic coverage level available to farmers for a nominal processing fee of $50 per crop per county, up to $100 per farmer per county. This catastrophic plan will protect against yield losses greater than 50 percent at a payment rate of 60 percent of the expected market price -- a level comparable to disaster relief programs in recent years. The processing fee may be waived for limited resource farmers.

Farmers may purchase additional insurance coverage providing higher yield or price protection levels for additional cost. Targeted subsidies are provided to encourage farmers to pursue these higher coverage levels.

3: **Linkage to farm programs:** To ensure wide participation, crop insurance coverage at the catastrophic level or above is linked to participation in Federal commodity support programs or Farmers Home Administration loans. This step should result in crop insurance participation rising from 33 percent to about 80 percent of insurable acres.

4: **Delivery:** Farmers may choose to obtain the catastrophic coverage either through a private reinsured company or through a USDA county office. Higher insurance coverages remain available only through private insurers.

5: **Industry competition:** Premium rates are restructured to reflect both direct premium subsidies and the insurers expense reimbursement allowance, a more realistic calculation. More-efficient companies will be allowed to pass along lowered overhead costs in reduced rates charged to farmers, creating a more competitive market environment.

6: **Uninsurable crops:** A standing disaster program would exist for crops not covered by crop insurance triggered, with payments triggered by area-wide loss levels and protection levels similar to those under the catastrophic insurance plan.

7. **Fiscal soundness:** The new catastrophic coverage will be governed by actual "APH" yields and all other program changes outlined in the "Blueprint for Financial Soundness."

8: **Cost:** The new program will cost about $8.1 billion for fiscal years 1995 through 1999. This represents a five-year savings of some $750 million compared to the projected cost of the current Federal crop insurance program plus the average annual cost for ad hoc crop loss disaster relief programs over the past decade.

SECTION-BY-SECTION ANALYSIS OF AMENDMENTS
TO FEDERAL CROP INSURANCE ACT

Section 2 contains the specific amendments to Title V of the Agricultural Adjustment Act of 1938 (the "Act") necessary to improve delivery, participation, and actuarial soundness of the Federal crop insurance program, and eliminate the need for ad hoc disaster legislation. Due to the large number and complexity of the amendments, the following analysis shall be conducted on a section-by section basis of the Act.

Section 505(a) provides for the Board of Directors (the "Board") for the Federal Crop Insurance Corporation (the "Corporation"). Subsection (a), as amended, eliminates the possibility of two positions on the Board being occupied by the same Under/Assistant Secretary and removes the requirement that the Under/Assistant Secretaries named to the Board be responsible for the farm credit programs. This is to conform to the Secretary's proposed reorganization legislation combining several agencies, including the Agricultural Stabilization and Conservation Service, the Farmers Home Administration and the Federal Crop Insurance Corporation, into a single Farm Service Agency.

Section 506 is amended by adding a new subsection (j) that would provide the Corporation with the authority to settle and adjust any claims brought by or against it. Taking into consideration the sheer number of insurance contracts in existence, this amendment provides the Corporation with the authority to avoid the existing inefficient and ineffective procedures where the Corporation must obtain authorization from the Department of Justice to settle or adjust claims in excess of the amount set under the Debt Collection Act.

Section 506 is amended by redesignating the subsections to conform to the addition of the new subsection (j).

Section 506(l), as redesignated, provides the Corporation with the authority to enter into contracts, agreements and regulations necessary to carry out its business and it preempts state or local laws to the extent they are inconsistent. "Regulations" were added to the section to ensure a nation-wide consistency of the program by precluding states from piece-meal enactment of laws that could thwart the national goals and mandates of the Federal crop insurance program.

Section 506(n), as redesignated, provides for the imposition of penalties when false or inaccurate information is provided to the Corporation and permits the imposition of a civil fine and a disqualification from purchasing the catastrophic risk protection coverage and noninsured assistance of up to two years. This is the maximum disqualification that has been historically imposed under the price support, product adjustment, and disaster programs of the Commodity Credit Corporation (CCC). Since participation in the price support and product adjustment

programs is linked to the purchase of catastrophic risk protection, disqualification for catastrophic risk protection is now consistent with the disqualification under the price support and product adjustment programs. Disqualification from any other benefit under this title is for a period not to exceed 10 years.

Section 506(o), as redesignated, requires that the Corporation take such actions as necessary to achieve actuarial soundness and permits the Corporation to determine who qualifies as a beginning farmer for the purposes of instituting procedures to document actual production histories in order to establish yields that more accurately reflect the risk.

Section 506(p) is from the present section 516(b) and authorizes the Secretary and the Corporation to issue any regulations necessary to carry out the provisions of the title. Since it enumerates a power of the Corporation, it is more appropriately located in section 506.

Section 506(q) is added as a new subsection that appropriates money to carry out the purpose of the insurance fund, without fiscal year limitation.

Section 507(a) removes a reference to county crop insurance committeemen since there are no longer county crop insurance committees.

Section 507(c) authorizes the Corporation to use and contract with committees and associations, private insurance companies, private rating bureaus and other organizations to avoid duplication of services available in the private sector. The Corporation is authorized to reimburse their administrative and program expenses. Compensation of agents and brokers are no longer paid from producer premiums. Compensation for private insurance companies has been moved to section 506(d) to reflect other amendments to the Act such as catastrophic risk protection coverage premium paid by the Corporation, operating and administrative expenses included in the premium and the different levels of subsidies that are provided for specific levels of coverage. Further, that portion of subsection (c) that provides indemnification for agents and brokers is no longer necessary since any claim arising under this Act must now be brought against the Corporation in the Federal district court pursuant to section 508(i), as amended.

Section 507(d) authorizes the Secretary to allot or transfer funds available through section 516 to other state or federal agencies as necessary to carry out the provisions of this title. The provision that employees or agencies responsible for administering the title shall be designated by and answerable to the Corporation without intervention of any intermediate office

has been deleted to conform to the Secretary's proposed reorganization legislation.

Section 508, as amended, provides the authority and procedures for the Corporation to offer crop insurance under both a catastrophic risk protection plan and additional coverages.

Section 508(a) maintains the existing authority for the Corporation, however, insurable causes of losses have been amended to specify only losses caused by drought, flood or other natural disaster as determined by the Secretary. The provisions that require the Corporation to offer loss in yield protection at 75 per centum of the recorded or appraised average yield, the use of ASCS yields, prohibition against the Corporation offering in excess of 75 per centum of the recorded or appraised average yield, the provision that insurance not be provided on any agricultural commodity in any county in which the Board determines that the income from such commodity constitutes an unimportant part of the total agricultural income of the county, and the requirement that the Corporation shall report annually to the Congress have been omitted. The other provisions of this subsection have been moved for clarification and to reflect the different programs offered under the catastrophic risk protection program and additional coverage that can be purchased from private insurance providers. These moved provisions may have been modified to reflect the proposed reform and the sections where they have been placed will reflect those changes.

Section 508(b)(1) authorizes the Corporation to offer a catastrophic risk protection plan that would indemnify producers for loss in yield or prevented plantings because of drought, flood, or natural disasters.

Section 508(b)(2) provides coverage for the catastrophic risk protection program at 50 per centum loss in yield, indemnified at 60 percent of the expected market price, or comparable coverage determined by the Corporation.

Section 508(b)(3) authorizes producers to base their catastrophic risk protection coverage on either an individual yield and loss basis or area yield and loss basis when both are offered by the Corporation.

Section 508(b)(4) authorizes the Corporation to charge producers an administrative fee for their catastrophic risk protection coverage of $50 per crop per county, not to exceed $100 per producer per county. This administrative fee is paid at the service point, the USDA office or the private insurance provider. The fee is waived for limited resource farmers and when the producer purchases additional coverage at or above 65 per centum of the recorded or appraised average yield and 100 percent of the expected market price, as offered by the private insurance

provider. Fees collected are available for salaries and expenses, subject to appropriations.

Section 508(b)(5) requires that, if the producer participates in the catastrophic risk protection coverage program, he must participate for that crop on all insurable land in the county.

Section 508(b)(6) requires that producers purchase catastrophic coverage for any crop that has or is expected to contribute 10 per centum or more of the total expected value of all crops grown by the producer in order to participate in any price support, production adjustment or conservation program administered by USDA for any crop or to participate in any Farmers Home Administration loan program.

Section 508(b)(7) is from the present subsection (a) and only provides the Corporation with the authority to limit insurance on the basis of the risk for catastrophic risk protection coverage; the Corporation may not refuse insurance.

Section 508(c)(1) provides the Corporation with the authority to offer plans of insurance providing coverage greater than the catastrophic risk protection and sold only through private insurance providers if private insurance is available. If the producer has already applied at a USDA service point, his file shall be transferred to his chosen private provider. If the producer purchases coverage at 65 per centum of more of the recorded or appraised average yield and 100 percent of the expected market price, his administrative fee will be refunded.

Section 508(c)(2) gives the producer the option of basing his coverage on either an individual or on an area yield, when both options are offered.

Section 508(c)(3) provides that the level of coverage is dollar denominated and permits the producer to purchase any level. The individual yield cannot exceed 85 percent and the area yield cannot exceed 95 percent.

Section 508(c)(4) is the present subsection (a) and only applies to the additional coverage plans. It provides that the Corporation has the authority to offer a price level for each commodity at not less than the projected market price. As amended, the Corporation may offer a price level based on the actual market price at the time of harvest.

Section 508(c)(5) is from the present subsection (a) and only applies to the additional coverage plans. It provides that producers may choose any price election that is equal or less than the price established by the Board. Further, as amended, the Corporation has the authority to set minimum price election levels.

Section 508(c)(6) is from the present subsection (e)(2) and amends the formula to give the Corporation the discretion in determining the premium deduction when the insured elects to exclude hail and fire coverage and obtain that coverage from a private insurance provider. The producer must purchase coverage of at least 65 per centum or more of the recorded or appraised average yield and 100 percent of the expected market price, or an equivalent coverage, to be eligible.

Section 508(c)(7) is from the present subsection (e)(5).

Section 508(c)(8) is from the present subsection (a) and applies only to additional coverage.

Section 508(d)(1) is from the present subsection (e)(1) and provides the Corporation with the authority to set premiums for all plans of insurance based on actuarial sufficiency.

Section 508(d)(1)(A) stipulates that the premiums for catastrophic risk protection will be sufficient to cover anticipated losses and a reasonable reserve. Operating and administrative expenses are not included in the premium.

Section 508(d)(1)(B) stipulates that premiums for coverages greater that catastrophic risk protection but less that 65 per centum of the recorded or appraised average yield and 100 percent of the expected market price, or an equivalent coverage, will be sufficient to cover anticipates losses, a reasonable reserve, and an amount for operating and administrative expenses that is less than the amount established by for coverage at 65 per centum of the recorded or appraised average yield and 100 percent of the expected market price.

Section 508(d)(1)(C) stipulates that premiums for coverages at or greater than 65 per centum of the recorded or appraised average yield and 100 percent of the expected market price, or an equivalent coverage, will be sufficient to cover anticipates losses, a reasonable reserve, and an amount for operating and administrative expenses as determined by the Corporation on an industry wide basis as a percent of the total premium.

Section 508(d)(2) is from the present subsection (h) and authorizes the Corporation to pay a premium subsidy. The amount of subsidy is dependent on the level of coverage.

Section 508(d)(2)(A) stipulates that for catastrophic risk protection, the subsidy will equal the amount of the premium established in subsection (d)(1)(A).

Section 508(d)(2)(B) stipulates that for coverages greater that catastrophic risk protection but less that 65 per centum of the recorded or appraised average yield and 100 percent of the

expected market price, the subsidy will equal the amount of premium established for catastrophic risk protection, a reasonable reserve, plus the amount of operating and administrative expenses established in subsection (d)(1)(B).

Section 508(d)(2)(C) stipulates that for coverages at or greater than 65 per centum of the recorded or appraised average yield and 100 percent of the expected market price, the subsidy shall equal the amount of premium established for 50 per centum loss at 75 percent of the expected market price, a reasonable reserve, plus the amount of operating and administrative expenses established in subsection (d)(1)(C).

Section 508(d)(3) provides the authority for the private insurance company to pass on any savings in expense reimbursement to the producer by reducing premiums, as long as approved by the Corporation.

Section 508(e)(1) mandates that producers purchase their insurance and provide all necessary information and documents before the sales closing date for the crop. The Corporation has the authority to set the sales closing dates and must balance the need for convenience to the producer in obtaining benefits under price support and production adjustment programs and the goal of actuarial soundness.

Section 508(e)(2) requires the producer to provide acceptable records of previous acreage and yields or accept a Corporation determined yield.

Section 508(e)(3) requires the producer to report any acreage planted and prevented from planting by the designated acreage reporting date for the crop and location.

Section 508(f)(1) provides the Corporation with the authority to implement underwriting rules to ensure that yield coverage is provided for all participants in the crop insurance program.

Section 508(f)(2)(A)(i) is from the present section 508A(b)(1)(A)(ii) and authorizes the Corporation to utilize actual production history to determine the yield coverage. The producer provides records of his actual production for at least the previous 4 continuous crop years, eventually increasing the database of actual production records to 10 continuous crop years.

Section 508(f)(2)(A)(ii) is from the present section 508A(b)(1)(A)(iii) and authorizes the Corporation to utilize 65 percent of the transitional yield when the producer fails to submit adequate documentation of his crop history.

Section 508(f)(2)(B) is from the present subsection (n) and authorizes the Corporation to offer crop insurance based on an area yield.

Section 508(f)(2)(C) is from present section 508A(1)(B) and is modified to permit the producer to choose either an individual or an area yield on a commodity by commodity basis.

Section 508(f)(2)(D) is from the present section 508A(c)(1) and requires the Corporation to provide adequate notice to producers when the yield coverage provisions are effective before the application period.

Section 508(g)(1), as redesignated, is from the present subsection (b)(1) and permits persons to submit other insurance policies or provisions and rates or premiums in addition to any forms or policies the Board may require under subsection (c).

Section 508(g)(2), as redesignated, is from the present subsection (b)(2) and omits all reference to ASCS adjusted yield and deletes the authority to base policies on alternative factors of loss such as the average loss rate.

Section 508(g)(3), as redesignated, is from the present subsection (b)(3) and authorizes the Board to review and approve any policies or other materials submitted under this subsection.

Section 508(g)(4), as redesignated, is from the present subsection (b)(4) and modifies it to require the Corporation to publish any policies, provisions of policies and rates in the Federal Register as a notice and made available to all persons contracting for reinsurance under the same terms as the submitting party. The present authority requires that the policy be published as a rule.

Section 508(i), as redesignated, is from the present subsection (f) and authorizes the Corporation provide for the adjustment and payment of claims for losses. If a claim for an indemnity is denied, suit shall be brought against the Corporation and the private insurance provider in the Federal district court in which the farm is located.

Section 508(j), as redesignated, is from the present subsection (h) and directs the Corporation to provide reinsurance under such terms as the Board determines are consistent with subsection (b) and (c) of this section. The Corporation has the discretion to define "insurers". The provision regarding subsidies has been moved to subsection (d)(2). The provision regarding the use of private insurance providers and their compensation has been omitted.

Section 508(k), as redesignated, is from the present subsection (i) and authorizes the Corporation to offer plans of insurance in other areas within the control of the United States.

Section 508(n), as redesignated, is from the present subsection (m) and requires the Corporation to make available to producers the current information pertaining to all aspects of Federal crop insurance and a listing of insurance agents.

Section 511 is amended to provide that contracts of insurance and premiums are also exempt from state, county, municipal or local taxes.

Section 516(a) authorizes appropriations, including funds collected as administrative fees, for the Corporation to pay its operating and administrative expenses.

Section 516(b) establishes an insurance fund as a repository of moneys received from premium income, reinsurance, borrowing, and appropriations authorized under this Act. The Corporation is authorized to pay amounts due under its reinsurance agreements from this fund, including premium subsidies.

Section 520 is amended to establish that producers shall be eligible for catastrophic risk protection coverage as long as they meet the definition of a "person" as determined by the Secretary. For other plans of insurance, the producer must be at least eighteen years old and have a bona fide insurable interest in the crop.

Section 3 creates a new section to authorize the Secretary to establish, as his discretion, an advisory committee made up of the Manager of the Corporation, the Secretary or his designee, and representatives from insurance companies and agents, farms producer organizations, experts on agronomic practices and banking and lending institutions. The members shall serve for up to two years and shall advise the Secretary on the implementation of the Act and other insurance matters as determined by the Manager. This committee shall file annual reports to the Secretary specifying the progress toward implementation of the Act, actuarial soundness and participation in the programs.

Section 4 creates a new section that will replace existing standing ad hoc disaster with a noninsured assistance program that will cover those crops for which crop insurance is not offered by the Corporation.

Section 522(a)(1) authorizes the Corporation to establish the noninsured assistance program. Covered will be all commercial crops for which catastrophic risk protection coverage is not offered but is produced for food or fiber. Livestock is expressly excluded. The program shall not cover losses due to

neglect or malfeasance, failure to reseed if customary, or failure to follow good farming practices.

Section 522(a)(2) requires applications be timely filed. The Corporation shall set the deadlines in its regulations to maximize flexibility.

Section 522(a)(3) requires the producer provide acceptable records of previous production or accept a yield set by the Corporation.

Section 522(a)(4) requires the producer to report acreage planted or prevented from planting by the acreage reporting date.

Section 522(a)(5) provides that an individual producer shall not be eligible for assistance unless the area average yield falls below 65 percent. The Corporation has the authority to determine what constitutes an area.

Section 522(a)(6) authorizes the Corporation to make prevented planting payments if he is prevented from planting more than 35 percent of the intended acreage because of drought, flood or other natural disaster.

Section 522(a)(7) authorizes the Corporation to make reduced yield payments if the producer's harvest is less than 50 percent of the area yield, factored for the producer's interest in the crop.

Section 522(a)(8) specifies that persons with gross revenues of greater than $2,000,000 annually are not eligible for noninsured assistance.

Section 522(b) specifies that if the producer is eligible for a noninsured assistance payment, payments will be made for losses greater than 50 percent of the established yield at 60 percent of the average market price, or any comparable coverage set by the Corporation.

Section 522(c) authorizes the Corporation to establish yields. If the producer can produce satisfactory evidence of his actual production history, it shall be his yield. If the producer cannot prove his actual production history, his yield shall be not less than 65 percent of the transitional yield.

Section 522(d) authorizes the Corporation to pay all losses under this section from the insurance fund and reimburse the fund from subsequent appropriations. These losses shall not be included in the calculations of producer premiums.

Section 522(e) limits the payments that a person can receive under this section to $100,000 annually. A "person" shall be defined in accordance with the Food Security Act of 1985.

Section 5 makes conforming amendments to the Agricultural Act of 1949, as amended, by striking sections 101B(c)(1)(F), 103B(C)(1)(F), 105B(c)(1)(G), 107B(c)(1)(G), and 208 that authorize standing ad hoc disaster assistance. Further, sections 101B(c)(2), 103(h), 103B(c)(2), 105(c)(2), 107B(c)(2), 108B, 205, 206, and 207 have been amended conform to the requirement that producers purchase at least catastrophic risk protection coverage as a condition of receiving any benefits under the price support, production adjustment or conservation programs administered by USDA or loan programs administered by Farmers Home Administration. Conforming amendments have also been made to the Food, Agriculture, Conservation, and Trade Act of 1990 to strike Chapters 1,2, and 3 of Subtitle B of Title XXII that authorize standing ad hoc disaster assistance. These amendments are effective the date of enactment of the Act. Section 251 of the Balanced Budget and Emergency Control Act of 1985 is amended to prohibit the designation of any agricultural crop disaster assistance as an emergency.

Section 6 states that sections 2, 3, and 4 becomes effective the crop year following the date of enactment of this Act.

AN ACT

To reform the Federal crop insurance program and for other purposes.

Be it enacted by the Senate and the House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Federal Crop Insurance Reform Act of 1994".

SECTION 2. CROP INSURANCE AMENDMENTS.

(a) Section 505 of Title V of the Agricultural Adjustment Act of 1938 (7 U.S.C. § 1505) is amended--

(1) by striking "the" after "Federal crop insurance program," and inserting "one additional"; and

(2) by striking "responsible for the farm credit programs of the Department of Agriculture" and inserting "as designated by the Secretary".

(b) Section 506 of Title V of the Agricultural Adjustment Act of 1938 (7 U.S.C. § 1506) is amended--

(1) by redesignating subsections (j), (k), (l), (m), and (n) as subsections (k), (l), (m), (n), and (o), respectively;

(2) by inserting after subsection (i) the following new subsection:

"(j) Settling Claims.-- The Corporation shall have the authority to make final and conclusive settlement and adjustment of any claims by or against the Corporation or the account of its fiscal officers.";

(3) in subsection (l) (as redesignated), by striking

"contracts or agreements" each place it appears and inserting "contracts, agreements, or regulations";

(4) in subsection (n)(1) (as redesignated), by striking paragraph (B) and inserting the following new paragraph:

"(B) disqualify the person from purchasing catastrophic risk protection or receiving noninsured assistance for a period not to exceed 2 years and from receiving any other benefit under this title for a period not to exceed 10 years.";

(5) in subsection (o) (as redesignated), by striking paragraph (1) and inserting the following new paragraph:

"(1) instituting appropriate requirements for documentation of the actual production history of insured producers to establish recorded or appraised yields for Federal crop insurance coverage that more accurately reflect the associated actuarial risk. The Corporation may not carry out this paragraph in a manner that would prevent beginning farmers, as determined by the Secretary, from obtaining Federal crop insurance.";

(6) by adding at the end thereof the following new subsections:

"(p) Regulations.-- The Secretary and the Corporation, respectively, are authorized to issue regulations as may be necessary to carry out the provisions of this title.

"(q) Source of Funding.-- There is hereby appropriated, without fiscal year limitation, such sums as may be necessary to carry out the purpose of the insurance fund.

(c) Section 507 of Title V of the Agricultural Adjustment

Act of 1938 (7 U.S.C. § 1507) is amended--

(1) in subsection (a), by striking ", and county crop insurance committeemen"; and

(2) in subsection (c), by striking the words beginning with ", in which case the agent or broker" through "the agent or broker has caused the error or omission"; and

(3) in subsection (d), by replacing the comma with a period after the words "section 516 of this Act", and by deleting the remainder of the subsection.".

(d) Section 508 of Title V of the Agricultural Adjustment Act of 1938 (7 U.S.C. § 1508) is amended--

(1) by striking subsection (a) and inserting the following new subsection:

"(a) Authority to offer insurance.--

"If sufficient actuarial data are available, as determined by the Board, the Corporation may insure or provide reinsurance for insurers of producers of agricultural commodities grown in the United States under any plan or plans of insurance determined by the Board to be adapted to the agricultural commodity involved. To qualify for coverage under these plans of insurance, the losses of the insured commodity shall be due to drought, flood or other natural disasters as determined by the Secretary. Except in the case of tobacco, insurance shall not extend beyond the period the insured commodity is in the field. For the purpose of the foregoing sentence, in the case of aquacultural species, the term field means the environment in which the commodity is

produced. Insurance provided under this subsection shall not cover losses due to: (i) the neglect or malfeasance of the producer; (ii) the failure of the producer to reseed to the same crop in those areas and under such circumstances where it is customary to so reseed; or (iii) the failure of the producer to follow good farming practices, as determined by the Corporation.";

(2) by striking subsections (c), (e), (g), (l) and (n);

(3) by redesignating subsections (b), (d), (f), (h), (i), (j), (k), and (m) as subsections (g), (h), (i), (j), (k), (l), (m), and (n) respectively;

(4) by inserting after subsection (a) the following new subsections:

"(b) Catastrophic risk protection.--

"(1) The Corporation shall offer a catastrophic risk protection plan that would indemnify producers for crop loss due to loss of yield and prevented planting when the producer is unable because of drought, flood or other natural disaster, as determined by the Secretary, to plant other crops for harvest on that acreage for that crop year.

"(2) Catastrophic risk protection shall offer the producer 50 per centum loss in yield coverage, on an area or individual yield basis, indemnified at 60 percent of the expected market price or a comparable coverage as determined by the Corporation.

"(3) Producers shall have the option of basing their

catastrophic coverage on either an individual yield and loss basis or on an area yield and loss basis when both options are offered by the Corporation.

"(4) In return for catastrophic risk protection, producers will be required to pay an administrative fee. The administrative fee shall be $50 per crop per county, not to exceed $100 per producer per county. The administrative fee shall be paid at the service point, the United States Department of Agriculture office or the approved private insurance provider, at the time of application. This administrative fee shall be waived for limited resource farmers, as defined by the Corporation, or in the event that the producer elects to purchase additional protection at 65 per centum or more of the recorded or appraised average yield and 100 percent of the expected market price, or an equivalent coverage, offered by approved crop insurance providers. Funds collected as administrative fees shall be available, subject to appropriations, for salaries and expenses.

"(5) Participation in the catastrophic risk coverage for any producer's crop on any land in the county requires participation for that producer's crop on all insurable land of the producer in the county.

"(6) To be eligible for any price support, production adjustment or conservation program administered by the U.S. Department of Agriculture for any crop, or for loans under

any program of the Farmers Home Administration or any successor agency, the producer must obtain at least the catastrophic level of insurance for all crops of economic significance grown on all farms in the county in which the producer has an interest, if insurance is available in the county for those crops. The term 'economic significance' shall mean any crop that has contributed, or is expected to contribute, 10 per centum or more of the total expected value of all crops grown by the producer.

"(7) The Board may limit insurance in any county or area, or on any farm, on the basis of the insurance risk involved.

"(c) Coverage levels generally.--

"(1) The Corporation shall offer plans of insurance providing levels of coverage greater than that available under catastrophic risk protection. Producers may only purchase these other plans from approved private insurance providers, if such private insurance is available. Nothing contained herein restricts the Corporation from offering insurance if coverage from private insurance providers is unavailable. If the producer has already applied for catastrophic risk protection at the United States Department of Agriculture office and elects to purchase additional coverage, the insurance file for that producer shall be transferred to the approved private insurance provider servicing the additional coverage policy and the

administrative fee for the crop for which additional coverage at 65 per centum or more of the recorded or appraised average yield and 100 percent of the expected market price, or an equivalent coverage, is obtained shall be refunded to the insured.

"(2) Producers shall have the option of purchasing additional coverage based on either an individual yield and loss basis or on an area yield and loss basis when both options are offered by the Corporation.

"(3) The level of coverage shall be dollar denominated and may be purchased at any level not to exceed 85 percent of the individual yield or 95 percent of the area yield, as determined by the Corporation.

"(4) The Corporation shall establish a price level for each commodity on which insurance is offered that:

"(A) shall not be less than the projected market price for the commodity as determined by the Corporation; or

"(B) at the discretion of the Corporation, may be based on the actual market price at the time of harvest, as determined by the Corporation.

"(5) Insurance coverage shall be made available to the producer on the basis of any price election which equals or is less than that established by the Board and the coverage shall be quoted in terms of dollars per acre: Provided, That the Corporation may establish minimum price elections below which levels of insurance shall not be offered.

"(6) For levels of coverage 65 per centum or more of the recorded or appraised average yield and 100 percent of the expected market price, or an equivalent coverage, the producer may elect to delete from the insurance coverage provided under this Act coverage against damage caused by fire and hail, provided an equivalent or greater dollar amount of coverage for damage caused by fire and hail is obtained from a private hail/fire insurance provider. Upon written notice of such election to the company issuing the policy providing coverage under this Act and submission of evidence of substitute coverage on the commodity insured, the producer's premium shall be reduced by an amount determined by the Corporation to be actuarially appropriate, taking into account the actuarial value of the remaining coverage provided by the Corporation. In no event shall the producer be given credit for an amount of premium determined to be greater than the actuarial value of the protection against losses caused by fire and hail that is included in the coverage under this Act for the crop.

"(7) The Board may enter into agreements with any State or agency of a State under which such State or agency may pay to the approved insurance provider an additional premium subsidy to further reduce the portion of the premium paid by farmers in such State.

"(8) The Board may limit or refuse insurance in any county or area, or on any farm, on the basis of the

insurance risk involved.

"(d) Premiums.--

"(1) The Corporation shall fix adequate premiums for all its plans of insurance at such rates as the Board deems actuarially sufficient to attain an expected loss ratio of not greater than 1.1.

"(A) For catastrophic risk protection coverage, the amount of premium shall be sufficient to cover anticipated losses and a reasonable reserve.

"(B) For levels of coverage below 65 per centum of the recorded or appraised average yield and 100 percent of the expected market price, or an equivalent coverage, but greater than catastrophic risk protection, the amount of premium shall be sufficient to cover anticipated losses, a reasonable reserve, and an amount for operating and administrative expenses, as determined by the Corporation, that is less than the amount established for coverage at 65 per centum and 100 percent of the expected market price, or an equivalent coverage.

"(C) For levels of coverage of at least 65 per centum of the recorded or appraised average yield and 100 percent of the expected market price, or an equivalent coverage, the amount of premium shall be sufficient to cover anticipated losses, a reasonable reserve, and an amount to pay the operating and administrative expenses as determined by the Corporation on an industry-wide basis as a percent of the

total premium.

"(2) For the purpose of encouraging the broadest possible participation, the Corporation shall pay a part of the premium equivalent to:

"(A) for catastrophic risk protection coverage, an amount equal to the premium established in paragraph (1)(A) of this section;

"(B) for levels of coverage below 65 per centum of the recorded or appraised average yield and 100 percent of the expected market price, or an equivalent coverage, but greater than catastrophic risk protection, the amount of premium established for catastrophic risk protection coverage, a reasonable reserve, plus the amount of operating and administrative expenses established in paragraph (1)(B) of this section.

"(C) for levels of coverage at or greater than 65 percent of the recorded and appraised yield and 100 percent of the expected market price, or an equivalent coverage, on an individual or area basis, an amount equal to the premium established for 50 per centum loss in yield indemnified at 75 percent of the expected market price, a reasonable reserve, plus the amount of operating and administrative expenses established in paragraph (1)(C) of this section.

"(3) If a private insurance provider determines that it may provide insurance more efficiently than the expense

reimbursement amount set by the Corporation, the private insurance provider, if approved by the Board, may reduce the premium charged the insured by the amount of such efficiency. Any such reductions shall be subject to the rules, limitations, and procedures established by the Corporation.

"(e) Eligibility.--

To participate in catastrophic risk protection coverage under this Act, producers may make application at the local United States Department of Agriculture office or to an approved private crop insurance provider. For all coverages, producers shall be required to:

"(1) purchase crop insurance on or before the sales closing date for the crop by providing the required information and executing the required documents. Such sales closing date shall be established by the Corporation to maximize convenience to producers in obtaining benefits under price and production adjustment programs of the Department whenever feasible; however, the Corporation will establish all sales closing dates to assure that the goal of actuarial soundness for the crop insurance program is met;

"(2) provide records, acceptable to the Corporation, of previous acreage and production or accept a Corporation determined yield; and

"(3) report acreage planted and prevented from planting by the designated acreage reporting date for that

crop and location as established by the Corporation.

"(f) Yield determinations.--

"(1) In general.--

The Corporation shall implement crop insurance underwriting rules that ensure that yield coverage, as specified in subsection (f)(2) of this section, is provided to all producers participating in the Federal crop insurance program.

"(2) Yield coverage plans.--

"(A) Actual production history.--

"(i) This plan uses the producer's actual production history for the 4 previous consecutive crop years without penalty, up to a production database of 10 consecutive years, subject to paragraph (ii), to determine yield coverage.

"(ii) If the producer does not submit adequate documentation of history for a crop, the producer shall be assigned, as the producer's farm program yield, not less than 65 percent of the transitional yield of the producer (adjusted to reflect actual production reflected in the records acceptable to the Corporation for continuous years), as specified in regulations issued by the Corporation based on production history requirements.

"(B) Area yield.--

The Corporation may offer a crop insurance plan

based on an area yield that allows an insured producer to qualify for an indemnity if a loss has occurred in an area, as specified by the Corporation, in which the farm of the producer is located. Under an area yield plan, an insured producer shall be allowed to select the level of area production at which an indemnity will be paid consistent with the terms and conditions established by the Corporation.

"(C) Commodity-by-commodity basis.--

A producer may choose between either individual yield or area yield coverage, where available, on a commodity-by-commodity basis.

"(D) Notice.--

The Corporation shall ensure that, whenever the yield coverage provisions of this section are effective, producers are given adequate notice of such provisions in advance of the crop insurance application period for the crops to which such provisions first will apply.";

(5) in subsection (g) (as redesignated) --

(A) in paragraph (1), by striking "(a)" and inserting "(c)";

(B) by striking paragraph (2) and inserting the following new paragraph:

"(2) Preparation of policies.--A policy or other material submitted to the Board under this subsection may be prepared

without regard to the limitations contained in this title, including the requirements concerning the levels of coverage and rates and the requirement that a price level for each commodity insured must equal the projected market price for the commodity as established by the Board. Such policy may only be subsidized at an amount equivalent to coverage which is authorized under this title.";

(C) in paragraph (3) -

(i) by striking "taking into consideration the risks covered by the policy or other material";

(ii) by inserting after "more than one reinsurance agreement" the words "with the private insurance provider"; and

(iii) by inserting after "Title 5" the words "of the United States Code";

(D) by striking paragraph (4) and inserting the following new paragraph:

"(4) Required publication.--Any policies, provisions of policies, and rates approved under this subsection shall be published as a notice in the Federal Register and made available to all persons contracting with or reinsured by the Corporation under the same terms and conditions as between the Corporation and the submitting person.";

(6) by striking subsection (i) (as redesignated) and inserting the following new subsection:

"(i) Claims for losses.--The Corporation may provide for adjustment and payment of claims for losses as provided under subsection (a) of this section under rules prescribed by the Board. The rules prescribed by the Board shall establish standards to ensure that all claims for losses are adjusted, to the extent practicable, in a uniform and timely manner. In the event that any claim for indemnity is denied by the Corporation, an action on such claim may be brought against the Corporation and the insurance provider in the United States District Court for the district in which the insured farm is located: Provided, That no suit on such claim may be allowed under this section unless it shall have been brought within one year after the date when written notice of denial of the claim is provided to the claimant.";

(7) by striking subsection (j) (as redesignated) and inserting the following new subsection:

"(j) Reinsurance.--Notwithstanding any other provision of this title, the Corporation is directed, to the maximum extent practicable, to provide reinsurance upon such terms and conditions as the Board may determine to be consistent with subsections (b) and (c) of this section and sound reinsurance principles to insurers, as defined by the Corporation, that insure producers of any agricultural commodity under a plan or plans acceptable to the Corporation. The Corporation's reinsurance agreements with the reinsured companies shall require the reinsured companies to bear a sufficient share of any

potential loss under such agreement so as to ensure that the reinsured company will sell and service policies of insurance in a sound and prudent manner, taking into consideration the availability of private reinsurance.";

(8) in subsection (k) (as redesignated), by striking "provide" after "The Corporation may" and inserting "offer plans of";

(9) by striking subsection (n) (as redesignated) and inserting the following new subsection:

"(n) Information collection on crop insurance.-- The Corporation shall make available to producers through local offices of the Department of Agriculture--

"(1) current and complete information on all aspects of Federal crop insurance; and

"(2) a listing of insurance agents.".

(e) Section 508A of Title V of the Agricultural Adjustment Act of 1938 (7 U.S.C. § 1508A) is repealed.

(f) Section 511 of Title V of the Agricultural Adjustment Act of 1938 (7 U.S.C. § 1511) is amended by inserting "its contracts of insurance and premium thereon, whether insured directly or reinsured by the Corporation," after "The Corporation, including".

(g) Title V of the Agricultural Adjustment Act of 1938 is amended by striking section 516 and inserting the following new section:

"Sec. 516. Authorization of appropriations

"(a) Appropriations.--

"There are hereby authorized to be appropriated such sums as may be necessary, including funds collected as administrative fees, to cover the administrative and operating expenses of the Corporation.

"(b) Insurance fund.--

"There shall be established an insurance fund for deposit of premium income, income from reinsurance operations, and appropriations provided by this Act. The Corporation will pay amounts due under its reinsurance agreements with private insurance providers, including premium subsidies, from the fund.".

(h) Title V of the Agricultural Adjustment Act of 1938 is amended by striking section 520 and inserting the following new section:

"Sec. 520. Producer eligibility

"Except as otherwise provided in this title, no producer shall be denied insurance under this title if:

"(a) for purposes of catastrophic risk protection coverage, the producer meets the definition of person, as defined by the Secretary; and

"(b) for purposes of any other plan of insurance, the producer is eighteen years of age and has a bona fide insurable interest in a crop as an owner-operator, landlord, tenant, or sharecropper.".

SECTION 3. ADVISORY COMMITTEE.

Title V of the Agricultural Adjustment Act of 1938 is amended by adding the following new section:

"Section 521. Advisory Committee for Federal Crop Insurance

"(a) Establishment.-- The Secretary may establish within the Department of Agriculture a committee to be known as the Advisory Committee for Federal Crop Insurance which shall remain in existence until September 30, 1998.

"(b) Membership.-- The Advisory Committee shall be composed of the Manager of the Corporation, the Secretary or his designee, and not less than 10 representatives of organizations or agencies involved with the Federal crop insurance program, which may include the following: insurance companies; insurance agents; farm producer organizations; experts on agronomic practices; and banking and lending institutions.

"(c) Administrative provisions.--

"(1) Terms.-- Members of the Advisory Committee shall be appointed by the Secretary for a term of up to two years from nominations made by the participating organizations. The terms of the members shall be staggered.

"(2) Chairperson.-- The Advisory Committee shall be chaired by the Manager of the Corporation.

"(3) Meetings.-- The Advisory Committee shall meet at least annually. The meetings of the Advisory Committee shall be publicly announced in advance and shall be open to the public. Appropriate records of the activities of the

Advisory Committee shall be kept and made available to the public on request.

"(d) Primary responsibility.-- The primary responsibility of the Advisory Committee shall be to advise the Secretary on the implementation of this Act and on other issues related to crop insurance, as determined by the Manager.

"(e) Reports.-- Not later than June 30 of each year, the Advisory Committee shall prepare, and submit to the Secretary, a report specifying its conclusions on--

"(1) the progress toward implementation of the provisions of this Act;

"(2) the actuarial soundness of the Federal crop insurance program; and

"(3) the rate of participation in both the catastrophic and the additional coverage programs.".

SECTION 4. NONINSURED ASSISTANCE.

Title V of the Agricultural Adjustment Act of 1938 is amended by adding the following new section:

"Section 522. Noninsured assistance program.--

"(a) Eligibility.--

"(1) A noninsured assistance program is established to provide coverage equivalent to the catastrophic risk protection insurance for crops for which catastrophic risk protection insurance is not available. Crops covered include all commercial crops and commodities for which

catastrophic risk protection coverage is not available and which are produced for food or fiber on a commercial basis but shall not include livestock. Noninsured assistance shall not cover losses due to: (i) the neglect or malfeasance of the producer; (ii) the failure of the producer to reseed to the same crop in those areas and under such circumstances where it is customary to so reseed; or (iii) the failure of the producer to follow good farming practices, as determined by the Corporation.

"(2) Producers shall make a timely application for noninsured assistance at the United States Department of Agriculture office.

"(3) Producers shall provide records, acceptable to the Corporation, of previous crop acreage and production or the producers shall accept a yield as determined by the Corporation.

"(4) Producers shall report acreage planted and prevented from being planted by the designated acreage reporting date for that crop and location as established by the Corporation.

"(5) Producers of non-program crops shall not be eligible for noninsured assistance unless the area, as determined by the Corporation, average yield, or an equivalent measure in the event yield data are not available, for that crop falls below 65 percent of the expected area yield as established by the Corporation.

"(6) The Corporation shall make a prevented planting noninsured assistance payment if the producer is prevented from planting more than 35 percent of the acreage intended for the crop because of drought, flood, or other natural disaster as determined by the Secretary.

"(7) If, because of drought, flood, or other natural disaster as determined by the Secretary, the total quantity of the crop that a producer is able to harvest on any farm is less than 50 percent of the expected area yield for the crop, as determined by the Corporation, factored for the producer's interest for the crop, the Corporation shall make a reduced yield noninsured assistance payment.

"(8) A person who has qualifying gross revenues in excess of $2,000,000 annually, as determined by the Secretary, shall not be eligible to receive any noninsured assistance payments. For purposes of this section, the term 'qualifying gross revenues' means--

"(A) if a majority of the person's gross revenue is received from farming, ranching and forestry operations, the gross revenue from the person's farming, ranching and forestry operations; and

"(B) if less than a majority of the person's gross revenue is received from farming, ranching and forestry operations, the person's gross revenue from all sources.

"(b) Payment rate.--

If the producer is eligible for noninsured assistance, payments shall be made for losses in excess of 50 percent of the established yield for the crop at 60 percent of the average market price for that crop or any comparable coverage as determined by the Corporation.

"(c) Farm yields.--

"(1) The Corporation shall establish noninsured assistance program farm yields for crops for the purposes of this section.

"(2) If the producer can provide satisfactory evidence of the producer's actual production history for the 4 previous consecutive crop years, up to a production data base of 10 consecutive crop years, the yield of the farm shall be based on such proven yield.

"(3) If the producer does not submit adequate documentation of such history for the crop, the producer shall be assigned as the producer's farm program yield not less than 65 percent of the transitional yield (adjusted to reflect actual experience), as specified in regulations issued by the Corporation based on production history requirements.

"(d) Payment of Losses.--

Payments for noninsured assistance losses under this section shall be made from the insurance fund and shall be reimbursed from appropriations provided in this Act. Such losses shall not be included in calculating the premiums

charged to producers for insurance.

"(e) Payment limitations.--

"(1) The total amount of payments that a person shall be entitled to receive annually under this section may not exceed $100,000; and

"(2) The Corporation shall issue regulations defining the term 'person' which shall conform, to the extent practicable, to the regulations defining 'person' issued under section 1001 of the Food Security Act of 1985 (7 U.S.C. § 1308).".

SECTION 5. CONFORMING AMENDMENTS.

(a) The Agricultural Act of 1949 is amended effective on the date of enactment of this Act-

(1) in section 101B (7 U.S.C. § 1441-2) --

(i) by striking subsection (c)(1)(F); and

(ii) in subsection (c) by striking paragraph (2) and inserting in lieu thereof the following:

"(2) Crop Insurance Requirement.-- As a condition of receiving any benefits (including payments) under this section, the producer must, if offered by the Federal Crop Insurance Corporation, obtain at least the catastrophic risk protection insurance coverage for the crop and crop year in which the benefit is sought.";

(2) in section 103(h) (7 U.S.C. § 1444), by adding at the end the following new paragraph:

"(17) As a condition of receiving any benefits (including

payments) under this section, the producer must, if offered by the Federal Crop Insurance Corporation, obtain at least the catastrophic risk protection insurance coverage for the crop and crop year in which the benefit is sought.";

(3) in section 103B (7 U.S.C. § 1444-2)--

(i) by striking subsection (c)(1)(F); and

(ii) in subsection (c) by striking paragraph (2) and inserting in lieu thereof the following:

"(2) Crop Insurance Requirement.-- As a condition of receiving any benefits (including payments) under this section, the producer must, if offered by the Federal Crop Insurance Corporation, obtain at least the catastrophic risk protection insurance coverage for the crop and crop year in which the benefit is sought.";

(4) in section 105B (7 U.S.C. § 1444f)--

(i) by striking subsection (c)(1)(G); and

(ii) in subsection (c) by striking paragraph (2) and inserting in lieu thereof the following:

"(2) Crop Insurance Requirement.-- As a condition of receiving any benefits (including payments) under this section, the producer must, if offered by the Federal Crop Insurance Corporation, obtain at least the catastrophic risk protection insurance coverage for the crop and crop year in which the benefit is sought.";

(5) in section 107B (7 U.S.C. § 1444b-3a)--

(i) by striking subsection (c)(1)(G); and

(ii) in subsection (c) by striking paragraph (2) and inserting in lieu thereof the following:

"(2) Crop Insurance Requirement.-- As a condition of receiving any benefits (including payments) under this section, the producer must, if offered by the Federal Crop Insurance Corporation, obtain at least the catastrophic risk protection insurance coverage for the crop and crop year in which the benefit is sought.";

(6) in section 108B (7 U.S.C. § 1445c-3), by adding at the end the following new subsection:

"(i) Crop Insurance Requirement.-- As a condition of receiving any benefits (including payments) under this section, the producer must, if offered by the Federal Crop Insurance Corporation, obtain at least the catastrophic risk protection insurance coverage for the crop and crop year in which the benefit is sought.";

(7) in section 205 (7 U.S.C. § 1446f), by adding at the end the following new subsection:

"(o) Crop Insurance Requirement.-- As a condition of receiving any benefits (including payments) under this section, the producer must, if offered by the Federal Crop Insurance Corporation, obtain at least the catastrophic risk protection insurance coverage for the crop and crop year in which the benefit is sought.";

(8) in section 206 (7 U.S.C. § 1446g), by adding at the end the following new subsection:

"(k) Crop Insurance Requirement.-- As a condition of receiving any benefits under this section, the producer must, if offered by the Federal Crop Insurance Corporation, obtain at least the catastrophic risk protection insurance coverage for the crop and crop year in which the benefit is sought.";

(9) in section 207 (7 U.S.C. § 1446h), by adding at the end the following new subsection:

"(k) Crop Insurance Requirement.-- As a condition of receiving any benefits (including payments) under this section, the producer must, if offered by the Federal Crop Insurance Corporation, obtain at least the catastrophic risk protection insurance coverage for the crop and crop year in which the benefit is sought."; and

(10) by repealing section 208 (7 U.S.C. § 1446i).

(b) The Food, Agriculture, Conservation, and Trade Act of 1990 is amended by striking Chapters 1, 2, and 3 of Subtitle B of Title XXII effective on the date of enactment of this Act.

(c) Section 251(b)(2)(D) of the Balanced Budget and Emergency Deficit Control Act of 1985 (2 U.S.C. § 901(b)(2)(D)), is amended effective on the date of enactment of this Act by striking subparagraph (i) and inserting the following new subparagraph:

"(i) If, for any fiscal year, appropriations for discretionary accounts are enacted that the President designates as emergency requirements and that Congress so designates in statute, the adjustments shall be the total of such

appropriations in discretionary accounts designated as emergency requirements and the outlays flowing in all years from such a appropriations: Provided, That this provision shall not apply to appropriations to cover agricultural crop disaster assistance.".

SECTION 6. EFFECTIVE DATE.

For the purposes of Sections 2, 3, and 4, these amendments take effect beginning with the crop year immediately following the date of enactment of this Act.

Major Points of the Blueprint for Financial Soundness

The **Blueprint for Financial Soundness** is a structured, comprehensive plan to achieve a long-term projected loss ratio of 1.1 by October 1995, as directed by the Omnibus Budget Reconciliation Act (OBRA) of 1993. FCIC is committed to achieving this goal because it is good public policy. A financially sound program is essential to maintaining public confidence in crop insurance. Sound management to achieve the goal will promote the long-term stability of the program and help maintain the financial stability of American Agriculture. The 1.1 loss-ratio goal recognizes that crop insurance differs from commercial insurance because it also serves social goals, not solely the business objective of maximizing profit.

The major initiatives outlined in the Blueprint are to:

A. **Develop More Accurate Insurance Yields**

B. **Develop a Catastrophic Yield Adjustment**

C. **Implement the Group Risk Plan (GRP)**

D. **Implement a Data Base of Taxpayer Identification Numbers**

E. **Expand the Non-standard Classification System (NCS)**

F. **Institute Premium Rate Adjustments**

G. **Improve Underwriting of Crop Insurance Contracts**

H. **Emphasize Program Compliance**

I. **Assure that Adequate Risk is Borne by the Commercial Insurance Industry**

J. **Improve Loss Adjustment**

K. **Improve Marketing**

L. **Expand Participation by Introducing New Products**

M. **Improve Accuracy of Other Program Variables: Unit division, Program dates, Staged guarantees, De minimus yields, Suspensions and debarment, Price elections.**

An in-depth discussion of each of these points, is contained in the **Blueprint for Financial Soundness** (available from USDA/FCIC).

BLUEPRINT FOR FINANCIAL SOUNDNESS

SCOPE AND PURPOSE

The Omnibus Budget Reconciliation Act of 1993 (OBRA 93) contains provisions concerning the Federal crop insurance program. These provisions direct the Federal Crop Insurance Corporation (FCIC) to take steps necessary to improve actuarial soundness of the Federal crop insurance program and to achieve, by the fiscal year beginning October 1, 1995, a projected overall loss ratio not to exceed 1.10 (110 percent) (section 1501 (a)).

Projected loss ratio (dollar amount of losses paid as a percent of the total premiums collected) is intended to be a performance standard, not an absolute ceiling for the operations of any particular crop year. Congress recognizes that adverse weather conditions (such as extreme drought or flood) will influence the financial results of each year's operations; however, when good and poor years are averaged over a long period of time (such as 50 to 100 years), the expectation must be that the program will operate with an average loss ratio of 1.10 or less. A period of time at least this long is needed to observe a range of production conditions that are likely to be encountered by farmers. Short time periods, such as 5 to 10 years, may encompass several favorable or unfavorable years, the frequency of which is atypical of the longer term. This is a primary reason that the risks covered by the Federal crop insurance program cannot be financed in a commercial insurance environment.

OBRA 93 directed FCIC to take the following actions to achieve this required improvement in the loss ratio:

- Institute rules for producers to demonstrate actual production histories in establishing yields for Federal crop insurance coverage that better reflect the associated actuarial risks.

- Establish in appropriate counties an optional "area yield" or "group risk" plan that allows producers to qualify for an indemnity if a loss occurs in a specified area in which the producer's farm is located.

- Create a nationwide database to track producer participation using social security account and employer identification numbers. Such a tracking system would facilitate better production documentation, high-risk producer identification, and assessment of insurance providers' performance.

- Take other measures authorized by law to improve the actuarial soundness of the Federal crop insurance program while maintaining fair and effective coverage for producers.

FCIC is committed to achieving these actions because it is good public policy. A financially sound program is essential to maintaining public confidence in crop insurance. Sound management to achieve these actions will promote long-term stability of the program and

facilitate the overall economic stability of the United States agricultural sector. Crop insurance differs from commercial insurance because it serves social goals, not solely the business objective of maximizing profit. A stable crop insurance system never developed in the private sector without government support because of the unique and widespread risks inherent in farming.

Section 1501 (c) (2) further directed the Department to issue for public comment a comprehensive plan or "blueprint" that identifies, among other things:

- Steps FCIC intends to take to achieve a projected overall loss ratio of no greater than 1.10 on and after October 1, 1995.

- Additional steps if further action is required, based upon actual program experience or unforeseen external circumstances.

- Modifications to be considered if initial actions to improve actuarial soundness work better than anticipated.

- Projections, assumptions, and analyses which underlie the FCIC conclusions that the above actions will achieve the required loss ratio within the stated deadline while maintaining fairness and effective coverage to agricultural producers, and which thereby demonstrate FCIC's compliance with the performance standard identified in section 1501 (a).

This document proposes a draft comprehensive **Blueprint for Financial Soundness**, as required by OBRA 93 for discussion and public comment. The plan has been developed with the guidance of various persons involved with crop insurance (producers, insurers, agents, academics, and others). The plan will be modified periodically to incorporate resulting analyses of program performance and the recommendations of interested parties as required by OBRA 93.

Actions identified herein result from internal analysis by FCIC and information previously provided to FCIC by numerous interested parties. These include the Commission for the Improvement of Crop Insurance (a Congressionally established work group in 1989 and 1990), various crop insurance industry organizations, members of Congress, agricultural producers, crop insurance agents and insurance companies, the General Accounting Office, and others. Information was not solicited specifically for this draft but was compiled from previous recommendations. Not all of the specific recommendations made by any or all of these groups are included herein. This document establishes initiatives to achieve the above actions.

Estimates of the financial impact of an action, based on available data and professional judgment, are provided whenever possible. Readers should recognize that these estimates are fluid due to the nature of the data and the ever-changing program. In particular, since FCIC

does not have a single aggregate mathematical or statistical model that describes its programs, estimates of financial impact are based on partial analysis which considers the effect of one particular action in the absence of any other action or initiative. Also, the exact steps to be taken under this Blueprint depend in part upon the public comment and recommendations received before investing resources in detailed studies of potential impacts. Readers are encouraged to provide information, rationale, and where possible, estimates of costs or potential savings.

In some cases the financial impact of an action may not be quantified. This does not mean the action is not important or that it cannot contribute to achievement of the goal. For example, enhanced management reporting systems do not produce a measurable financial impact. However, such systems can enhance FCIC's ability to estimate the potential impacts of program changes and assure that ongoing management decisions recognize the impact of the decision on future actions.

This document is divided into four main sections, which describe: (1) crop insurance program to provide context and background; (2) actions FCIC proposes as part of this plan to achieve the target loss ratio; (3) additional actions that FCIC may take if those described in Section II are not effective or that cannot be implemented due to unforeseen circumstances; and (4) changes FCIC will consider once the projected loss ratio achieves the targeted level of 1.10.

I. BACKGROUND OF THE CROP INSURANCE PROGRAM

A. Overview of Program Operations

Crop insurance is delivered primarily by commercial insurance companies that have entered into a cooperative financial arrangement (the Standard Reinsurance Agreement [SRA]) with FCIC. Under this arrangement, the company agrees to deliver an FCIC designed and priced product to eligible buyers. The company is responsible for all aspects of customer service, and guarantees payment of the insured person's share of the premium to FCIC. In return, FCIC reimburses the company for administrative expenses and requires the company (on a state basis) to share in insurance experience whether favorable or unfavorable. FCIC also provides stop loss reinsurance that limits the maximum loss the company can sustain.

A small and decreasing portion of the total sales is managed directly by FCIC through sales and service contractors. These contractors agree to sell an FCIC designed and priced product and to perform certain servicing functions related to the sale (such as determining the average yields). FCIC reimburses the contractor for administrative expenses associated with selling and servicing the product; however, FCIC is directly responsible for premium collection, loss adjustment, and payment of losses. These latter functions are the responsibility of the reinsured company under that delivery

system. FCIC intends to eliminate direct sales after the 1994 crop year because this system now delivers less than 10 percent of the total business, and maintaining a nationwide capability for delivery at an acceptable cost is difficult.

The crop insurance plan for most crops indemnifies insured persons for losses in yield exceeding a predetermined threshold amount. To establish this threshold an average yield is determined based on the individual's production history. The first portion of the loss (deductible of the insurance), equal to 25, 35, 50, or 65 percent of the average yield, must be sustained by the insured person. These are the choices of deductibles now offered by FCIC, and typically are described by the maximum loss in yield covered by the insurance; e.g., 75 percent coverage, 65 percent, etc. The 50 and 75 percent coverage levels are required by the Act to be available to all persons. The level of coverage is chosen by the insured individual.

The insured person also must choose a price at which the yield is valued for the purposes of computing the amount of premium and any applicable amount of loss; this variable is called the price election. FCIC must offer a price election that is not less than the anticipated market price at time of harvest. This determination is made well before the possibility of loss is known during the crop year. Otherwise, insured persons would choose low price elections if no loss is sustained (minimizes premium payments) the highest possible price election if a loss occurs (maximizes indemnities).

FCIC establishes premium rates for the various coverage levels, yields, crop types and farming practices (e.g., irrigated) for each county. All planted acres of the crop are covered by the insurance policy unless for some reason the acreage is uninsurable. The premium owed by the insured person is determined by multiplying the average yield per acre by the coverage level, multiplied by the number of acres planted, the price election, and the premium rate. For example, if the average yield is 100 bushels per acre, the coverage level is 65 percent, planted acres are 50, the price election is $2.25, and the premium rate is 5.2 percent, the premium is equal to 100 x 0.65 x 50 x $2.25 x 0.052, or $380.25. The potential indemnity in the event of a total loss is $7,312.50 (determined by multiplying the average yield, coverage level, planted acres, and price election).

A portion of the total premium is subsidized to encourage participation in the program. The subsidy is 30 percent of the total premium for coverage levels up to and including the 65 percent level. The subsidy for 75 percent level of coverage is equal to the dollar amount that would be paid at the 65 percent level of coverage. The premium subsidy for the above example would be $114.08; thus, the insured person would pay $266.17. The same $114.08 subsidy would be paid if the insured person chose the 75 percent coverage level.

In the event of a loss, the amount of production that was harvested, or that was determined should have been harvested, is measured by the insurer. An indemnity payment is made if the determined production is less than the total guarantee for the acreage (yield multiplied by coverage level and acres planted). For example, if the insured person harvests 1,000 bushels from 25 acres and does not harvest a potential yield of 10 bushels per acre from the remaining 25 acres, the total of the production to count is 1,250 bushels (1,000 bushels harvested plus 25 acres multiplied by 10 bushels). This is subtracted from the total bushel guarantee for the acreage (100 x 0.65 x 50, or 3,250 bushels), resulting in a loss of 2,000 bushels. The indemnity is equal to the number of lost bushels multiplied by the price election. For this example, the indemnity would be 2,000 bushels x $2.25, or $4,500.

Crop insurance does not guarantee revenue. As the above example illustrates, it provides an insurance indemnity only if production is less than the established guarantee. No protection is provided if the market price is less than the price election.

B. Legislative Background and Issues

Federal crop insurance was established as a pilot program in the 1930's. Prior to 1980, crop insurance was available only on major crops in major producing areas. The coverage level often was limited to 60 percent or less of a long-term average yield for an area. Congress amended the Act in 1980 to expand the scope and coverage of the program with the intent that it be the sole means of providing public disaster assistance to U.S. farmers. Participation in the program increased after the 1980 amendments, but remains below levels deemed necessary to be regarded as the principal vehicle for disaster assistance. Insured acreage peaked at about 40-45 percent of the total acreage planted to insurable crops in 1988-89, but more commonly has been in the 30-35 percent range. Losses also increased with the expansion of the program. The loss ratio has exceeded the break-even amount of 1.00 in every year since 1980. Cumulative losses for the years 1980-1992 were approximately $2.9 billion, with a cumulative loss ratio of about 1.45 for the 13 years.

Program participation is an issue influencing the Federal crop insurance program. Full participation (i.e., 100 percent of eligible acres insured) is the measure of program success that is accepted (at least implicitly) by some persons. This measure may not be the most appropriate. A rational decision to buy insurance of any kind must be based on the magnitude of the financial difficulties that accompany a loss. For example, buying collision coverage on a 15-year old automobile makes little financial sense. Similarly, buying insurance on a crop that contributes only a small portion of the expected income of the insured person may not make financial sense. Full participation in the crop insurance program may not represent an efficient use of the taxpayer's resources. However, participation must be high enough to minimize or

eliminate perceived needs to legislate disaster assistance funded under dire emergency provisions of the Budget Enforcement Act. The level of participation in the crop insurance program that maximizes returns to the public is not known, and is an area needing further definition.

Many losses paid in the 1980's and early 1990's were due to widespread disasters, the adverse financial effects of which Congress intended to mitigate under the Act. However, continuing loss ratios exceeding 100 percent, enactment of disaster assistance in nearly every year since 1988, and lower than desirable participation indicate that the public policy goals of the program have not been fully realized. The Secretary of Agriculture has proposed a reform of the crop insurance program to:

- Achieve actuarial soundness.
- Increase participation to levels that render ad hoc disaster legislation unnecessary.
- Eliminate incentives to enact ad hoc disaster assistance legislation.

The proposals contained in this Blueprint focus on these three areas that directly relate to the goal of achieving the targeted loss ratio. They are: (1) actuarial matters such as premium rates and yield guarantees, (2) underwriting matters such as terms and conditions of insurance policies, and (3) management issues such as compliance and risk-sharing arrangements with commercial insurers.

II. MANAGEMENT ACTIONS TO ACHIEVE A LOSS RATIO OF 1.10

A. Develop More Accurate Insurance Yields

The insurance yield may be the single most important factor in determining the success or failure of the crop insurance program. A yield that is too high compared to the productive potential of the person or land will increase the number of years that a loss is paid. An excessively high yield also increases the amount paid when a loss occurs. A yield that is too low will not effectively protect farmers from loss and, because it is regarded as insufficient, will not induce desired levels of participation.

From the 1985 through 1993 crop years, insured yields were based on a program called the Actual Production History (APH) Plan. The goal of this program was to obtain 10 previous yields to establish the insured yield for the next crop year. Proxy yields largely based on ASCS farm program payment yields or county averages were allowed whenever farmers would not or could not provide 10 years of history. Analysis by FCIC and others determined the proxy yields were benefiting farmers whose yields tended to be lower than average and discouraging farmers whose yields

tended to be above average. Consequently, a modified APH program that reduced the influence of the proxy yields was introduced beginning with the 1994 crop year; thus, a "ladder" was introduced into the proxy yields. Only 65 percent credit is given to the proxy yield if no actual yields are reported, 80 percent credit is given if one actual yield is reported, 90 percent if two actual yields are reported, and 100 percent if three actual yields are reported. The proxy yields are not used after four actual yields are available. The insured yield is a simple average of the 4 years of actual and modified proxy yields for the first 4 years, and then (after 4 years) is the simple average of the actual yields reported. Acquiring 10 years of production history remains the goal of the program. These revised procedures are the core of the initiatives to comply with the mandate of OBRA 93 to institute rules to demonstrate actual production histories.

The revised rules are expected to substantially reduce losses of the Federal crop insurance program. Analysis performed by FCIC indicates the new rules would reduce losses by 15 percent for corn, 22 percent for soybeans, and 18 percent for wheat. These analyses were based on simulations of loss histories using the rules for the two computational methods--the previous APH and the proposed modified-APH plans. The analyses encompassed nine states each for corn and soybeans and three states for wheat. These states and crops represented nearly 60 percent of the total premiums earned in 1990. The results indicated that the modified-APH rules would reduce losses by a weighted average of 19 percent and are believed to be representative for most crops.

The actual loss ratio for the 1990 crop year was 1.23. If the modified APH rules did reduce losses by an average of 19 percent, the loss ratio would have been 0.996. This would achieve significant compliance with the loss ratio target of 1.10.

Based on these results, FCIC implemented modified-APH for the 1994 crop year by:

- Promulgating regulations for the program during calendar year 1994.

- Measuring the impact of the modifications upon net program losses by calculating insured yields, premiums, and indemnities of policyholders under 1993 and 1994 rules.

- Where possible, determining whether the modified APH rules had the intended effect of providing a more accurate offer for farmers who previously elected not to purchase crop insurance.

- Determining whether the average number of yields reported for prior years has changed under the modified APH rules compared with APH rules for 1990 through 1993.

- Implementing a tracking system to assure that insurance experience remains associated with a person in future years (see item D below).

- Developing reporting processes to assure that the accuracy of yield determinations is continuously monitored and improved.

- Actions requiring analysis of the effects of the modified APH rules upon the accuracy of insured yields cannot be completed until losses from the 1994 crop year are processed. For wheat and other fall planted crops, such availability will occur by about the fourth calendar quarter of 1994. For spring planted crops, this does not occur until about the middle of the first calendar quarter of 1995.

B. Catastrophic Yield Adjustment

FCIC recognizes that the average of a series of observations as short as 4 years is subject to significant variations due to abnormally large or small yields during that time. For example, if a major disaster year such as 1993 is included in the 4 years, the procedure implicitly states that a similar year will occur once every 4 years. This is not likely. Thus, FCIC will examine certain adjustments to the modified-APH rules with a goal to assign more appropriate probabilities to the individual observations. These adjustments commonly are called catastrophic yield adjustments. However, just as the yields for 1 year may be abnormally low, they also may be abnormally high. Capping the abnormally high years may also be appropriate so that average yields are not excessively high due solely to a few observations.

FCIC will evaluate alternative methods to recognize catastrophic and unusually good crop years, and consider implementing appropriate adjustments to the modified-APH plan effective for the 1995 crop year.

FCIC believes that these actions to implement modified-APH will reduce the average loss ratio over time by 10-15 percentage points (e.g., from an average of 1.40 for several years to 1.25 to 1.30). This estimate is based on a conservative expectation of the actual results of the simulations described above.

C. Implement Group Risk Plan

FCIC is implementing a program of insurance that is based on the average yield of an area, not upon individual yield coverage as is offered under the traditional APH program. The area coverage is called the Group Risk Plan (GRP) by FCIC. GRP was introduced as a pilot program for the 1993 crop year for soybeans in 96 counties. It was expanded for the 1994 crop year to include seven additional crops encompassing 1,872 county crop programs (one crop in one county) in 27 states. Crops now included under GRP are barley (three states), corn (17 states), cotton (seven states), forage (two

states), grain sorghum (four states), peanuts (four states), soybeans (24 states), and wheat (eight states).

The GRP is intended to protect the insured person against the financial consequences of a disaster that strikes all or nearly all farmers in an area. It sets an expected county yield for each year based on historical yields, adjusted for any trends. Whenever the actual county average yield for the year is less than the expected county yield by a predetermined amount, an indemnity is paid. The principal differences of the GRP compared to traditional individual coverage are:

- Coverage is based on a trend projected yield, which probably will exceed the average yield of all farmers insured under individual yield coverage if there is a positive trend in yields for the area.

- Higher coverage levels (deductibles are as low as 10 percent) at affordable premium rates can be sold.

Thus, in the proper circumstances, GRP will offer risk protection that may be better than the individual coverage, and may do so at a lower cost.

GRP has characteristics that make it unsuitable for managing the adverse financial consequences of crop loss in certain circumstances. A farmer's yield each year must change in the same direction and by about the same amount as the county yield if it is to be fully effective coverage for the individual. For example, if the county's yield decreases by 25 percent from the expected yield for that year, the farmer's yield also should decline by about 25 percent from the yield he or she would have expected. In financial market terms, the "beta" of the farmer's yields and the county yields should be near 1.00.

Adequate data are a limitation to further significant expansion of GRP. The concept as presently developed uses many years (30 or more) of county yields. These data are routinely available only for counties in which the crop has been grown in commercially significant quantities. Weather data and crop growth models may permit expansion into counties in which the historical yield data are not available, but research is needed to develop and test these approaches. Further, acceptance of GRP by bankers as collateral for loans is yet to be determined.

Significant expansion of GRP is not anticipated until its contributions to agricultural risk management can be measured. No estimates of savings can be attributed to GRP because customer acceptance is not known. Customer acceptance of the soybean GRP for the 1993 crop year was limited. Fewer than 500 policies (of nearly 700,000 total for the crop insurance program) were sold. Even if the plan improves the actuarial soundness of crop insurance, the present volume of business is not sufficient to make any noticeable difference in program results.

D. Implement Data Base of Taxpayer Identification Numbers

Amendments to the Federal Crop Insurance Act enacted in 1990 authorize FCIC to collect and use social security numbers and employer identification numbers to administer its programs. These regulations were appropriately approved and were published in the Federal Register in late 1992. OBRA 93 further directed FCIC to implement a database of these numbers for certain uses not later than the 1995 crop year.

FCIC implemented the database described above in January 1994, effective for the 1994 crop year. This database is used to locate production history that is not reported by a person, to assure that classifications assigned under the nonstandard classification system (NCS - see paragraph E below) are used for both the individual who accumulated the adverse history and any person having a significant beneficial interest in a crop produced by that person, and for other related purposes. In particular, further efforts will be made to accumulate information about persons involved in sales and servicing of crop insurance--agents, loss adjusters, and other insurance providers--so that their contributions to achieving the target loss ratio can be measured.

Implementing this database will make both modified-APH and the NCS more effective by permitting FCIC and reinsured companies to assure that all appropriate experience and premium rating factors are used. Incremental improvement in the loss ratio due to modified-APH and NCS is difficult to quantify. The database will enhance those programs as well as permit FCIC to systematically measure the performance of insurance providers for the first time.

FCIC will also use the social security numbers and employer identification numbers for the implementation of an Ineligible File Tracking System. This system will be used to restrict (through an automated environment) producers who have been declared ineligible to obtain benefits provided by the Federal crop insurance program. The FCIC expects to implement the Ineligible File Tracking System beginning with the 1995 fiscal year.

E. Expand the Nonstandard Classification System (NCS)

FCIC instituted the NCS for the 1990 crop year because evidence indicated that a small percentage of insured persons had losses in nearly every year. The losses paid to these persons far exceeded paid premiums. For various reasons, the insured yields for these individuals exceeded their apparent capabilities, and the premium rates were not representative of the risks posed by these persons. NCS was intended to reduce the insurance guarantee and increase the premium rate for such individuals. Modified-APH eliminates the need to reduce insured yields because the insured yield will be based

solely on actual yields when a person is selected for NCS. However, NCS will continue to increase the premium rates as appropriate for those individuals who persistently have losses.

The Agriculture, Rural Development, Food and Drug, and Related Agencies Appropriation Act for the 1994 fiscal year prohibited FCIC from using any funds appropriated to insure crops in certain counties unless an NCS program had been implemented in those counties. Counties were affected if the loss ratio, after applying the 1993 premium rates, was greater than 1.10 more than 70 percent of the years that the crop had been insured in that county. Approximately 2,100 county crop programs were affected by this provision.

For the 1994 crop year, NCS has been extended to 11 crops encompassing over 90 percent of the total value of insurance in force. Additionally, all of the county crop programs affected by the Appropriations language have been included under the NCS. Over 25,000 individuals (about 3.6 percent of all active policies for the 1993 crop year) were included under this program. Not all of these persons had been insured during the base period. NCS also extends to persons who participated in growing the crop in some way but who may not have been insured. These persons also are classified under NCS so that the acreage cannot simply be insured under a different name to avoid the NCS classification.

In 1993, FCIC commissioned a study of the NCS to determine its effectiveness. A draft report of that study indicates that the NCS reduced the loss ratio by 5 to 10 points. This report is undergoing final preparation as this **Blueprint for Financial Soundness** is finalized.

FCIC will expand the NCS program for the 1995 crop year. All eligible crops will be included, although greater flexibility in selections may be authorized whenever program factors that led to poor experience have been identified. NCS is not suited to certain insured crops (e.g., Texas citrus trees) that are subject to infrequent losses of great severity. The additional savings from NCS are likely to be small in terms of the total business because the crops that constitute the majority of premiums and losses already are included.

F. Institute Premium Rate Adjustments

Premium rates are essential to the success of the crop insurance program. Rates that are too low will not produce adequate income and will lead to persistent losses. High rates will, paradoxically, likely lead to the same outcome. Excessive premium rates discourage participation by a broadly based cross-section of the farming community. Instead, persons who are most likely to collect indemnities will buy, and it is not likely that rates can be increased as rapidly as the relative risk of the pool of insured persons increases.

FCIC has increased premium rates for all crops in a systematic fashion beginning with the 1991 crop year. Rates have increased as much as 70 percent for some crops in some counties from the 1991 to the 1994 crop years. Decreases of up to 20 percent have been made for some crops in counties with histories of low losses. By an amendment to the Act in 1990, Congress limited general premium rate increases to 20 percent annually.

The above statistics indicate the amounts that FCIC has increased the base premium rates. The average premium rate actually earned (actual premium paid divided by actual liability) may not have increased by the same magnitude for various reasons. Most importantly, insured persons may choose a lower coverage level when the rate increases. By doing so, they accept a lesser degree of protection but also pay a lower premium rate.

FCIC proposes to continue premium rate increases as needed to help achieve the required loss ratio. The rate increases made during 1991-1994 have done much to enhance the actuarial soundness of the program. However, the premium rates for some crops and areas of the country remain below the levels needed to achieve the overall 1.10 loss ratio target.

The impact of premium rate adjustments has been evaluated by using data for the 20 years from 1973-1992. The effectiveness of the adjustments was measured by applying the current 1993 premium rate levels to the historical period from 1973 and all subsequent years. The loss ratios were recalculated by using the revised premium amounts.

This method does not include any change in sales that may occur due to a higher or lower cost of insurance. It assumes the 20-year base period is adequate to measure actuarial performance, an assumption that may not be the most appropriate definition of actuarial soundness. Events such as a 1993 Midwestern flood may or may not be appropriate to include in the 20-year base period for a particular area of the country.

In 1993, seven crops (barley, corn, cotton, grain sorghum, oats, soybeans, and wheat) constituted 75 percent of total premiums. The loss ratio for 1980-1992 for these seven crops was 1.45, identical to the loss ratio for all insured crops for this same period. Thus, changes in premium rates for these crops should be representative of the changes that have been made for all crops in recent years. The premium rate changes for the seven crops through the 1994 crop year are estimated to have been adequate to reduce the 1980-1992 loss ratio from 1.45 to 1.08. This aggregate result meets the 1.10 standard required by OBRA 93, but only two of the seven crops individually meet this standard. Within each of these crops, many parts of the country will meet the standard but others will not. Hence, additional rate changes in 1995 and later years are appropriate.

FCIC recognizes that premium rate increases are an important component of a viable crop insurance program. It is also recognized that increasing premium rates to the levels suggested by the most recent 20 year experience may not be good public policy. Extremely high premium rates will preclude realization of the social benefits and public policy goals of the program because participation will be discouraged. If this happens, experience indicates that ad hoc disaster assistance will be enacted. Such assistance is less likely to satisfy social objectives with regard to maintaining rural communities and adequate supplies of food and fiber because it is uncertain for any particular year or region of the country. Thus, a catastrophic adjustment process may be needed to temper the influence of a year such as 1993. If the weather of 1993 truly is a 1 in 100 year event (or, as some have suggested, a 1 in 500 year event), its influence should be tempered in terms of the premium rates charged to insured persons.

In addition to changing premium rates as needed, FCIC proposes to take a number of additional actions to enhance the accuracy and adequacy of its actuarial activities. These include:

- Develop computer software and other tools to enhance the quality of the data used to establish premium rates and perform actuarial analyses ("STATPLAN" database, due for completion in October 1994)

- Plans to contract with a major actuarial consulting firm to review all aspects of FCIC's actuarial methods (targeted to be let in 1994).

- Enhance staff skills by additional training in analytical methods for existing personnel and more emphasis on recruitment of actuarial trainees (ongoing) for appropriate functional units.

- Continue to contract with external specialists such as the Economic Research Service, land grant universities, the Cooperative Extension Service, and others (ongoing).

- Develop models to measure sources of change in premium volumes and track the effects of premium rate changes as isolated from changes induced by factors such as price elections, coverage level choices, insured crops, and other factors that are not controllable by the rate-making function (development to begin immediately).

G. Improve Underwriting of Crop Insurance Contracts

Underwriting begins by establishing the basic terms and conditions of the coverage. These include defining conditions that result in a covered loss, measuring the amount of that loss, and defining the responsibilities of the insured and the insurer. Underwriting continues with proper classification of an insured risk. For example, planting crop B the year after crop A was grown on the same acreage may be riskier than if other crops

were grown the previous year. Some land, such as flood plains, is more prone to losses. Quality of management also is important. A farmer who is organized, plans, performs preventive maintenance on equipment, and performs field operations in a timely manner may minimize losses.

A comprehensive underwriting system requires effective risk management strategies and goals, standards, and documentation. Initiatives to improve underwriting that began in the early 1990's will be continued as part of the strategy detailed in this Blueprint. The following specific actions will be pursued:

- Fully automate the actuarial documents to facilitate more comprehensive underwriting at the point of sale and to verify the classification of risk in an automated environment (completed by the 1996 crop year).

- Develop standards and classification systems to assess and classify individual risk, including completion of research intended to develop a "scoring model" for risk that is based on measurable attributes of a person or situation similar to a credit rating model (for implementation by crop year 1996 if this model is feasible).

- Continue to rewrite crop insurance policies to better describe the insurance coverage and limitations and to reduce vulnerabilities to actuarial soundness that exist due to imprecise, unclear, or omitted terms and conditions (ongoing, with major crops scheduled for the 1995 crop year).

- Encourage development of supplemental or alternative insurance coverages authorized by section 508(b) of the Act so that coverage may be improved with most of the risk remaining in the commercial sector.

Improved underwriting will improve program performance. However, meaningful measures to quantify possible benefits are not readily available. For this reason, FCIC cannot attribute a specific dollar amount to the benefits of improved actuarial systems and crop insurance policies.

H. Emphasize Program Compliance

The FCIC Compliance function is designed to confirm that the Federal crop insurance program is operated and delivered as intended. Through internal reviews based on generally accepted auditing principles, it assures that program controls are in place against excess losses due to waste, fraud and abuse. Compliance emphasis will focus on:

1. **Program Delivery**. Beginning in 1987, the Compliance staff conducted reviews of program delivery to assess compliance with regulations, policy, and procedure.

That year, according to GAO and OIG audits, errors in claims payment represented an estimated 15 percent of all losses paid equaling $55 million of taxpayer dollars. Since that time, Compliance efforts have reduced these errors to approximately 5 percent of indemnities but still need continued improvement. Losses due to claim payment errors are not included in underwriting calculations of risk, so this reduction in excess losses has a direct and immediate impact of lowering the program loss ratio without increasing program cost or premium rates.

To further reduce claims overpayment the Compliance Staff will review the entire operations of each delivery company in coordinated nationwide reviews. The review methodology was recently revised to reflect generally accepted auditing principles and statistically projectable sampling techniques.

Beginning with the 1995 crop year, Compliance requirements will be expanded to define specific quality control and performance measurement processes for each delivery company. Policy service error rates will be monitored. The performance of each company will then be compared to an established national standard.

2. **Program Performance**. Compliance reviews for several years have shown that a proportion of the excess losses are attributable to features in program construction that produce unintended results. The Compliance Staff will conduct program performance reviews that assess regulations, policies and procedures designed to prevent waste, fraud, and abuse and that the program, policies, and procedures perform as intended.

   As an example, in 1989 GAO claims that construction of policy language in the California Safflower program alone resulted in approximately $20 million in excess losses. It is not possible to determine how much of FCIC losses may be attributable to unintended features of program construction. However, recent program performance pilot reviews of the peanut program and regional irrigated practices resulted in an estimated 4 to 10 percent reduction in losses for those areas that may otherwise have gone undetected.

   For the past several years Compliance has conducted ad hoc program reviews on topical issues. These reviews will be expanded to identify and target reviews for crop insurance programs with the greatest potential vulnerability.

3. **Fraud Prevention.** The risk of fraud is particularly acute in the insurance industry. Estimates for property-casualty insurance indicate insurance fraud may represent as much as 15 percent of all losses paid. Recent efforts at crop insurance fraud detection and subsequent prosecution have been increasingly successful. However, after-the-fact controls on program abuse are not fully effective. Compliance will work with the delivery companies to focus on practical, cost efficient fraud prevention. Compliance operations, program performance, and complaint reviews

will emphasize identifying systemic vulnerabilities and assessing program safeguards. Discrepancies noted in review findings will be evaluated to determine the underlying causes.

Emphasis also will be placed on measures to control program abuse that include strict contract enforcement and pro-active policy analyses that identifies potential abuse and targets additional claims review. These measures will be coupled with the aggressive implementation of civil sanctions, agent/loss adjuster debarment, and designating producer ineligibility in findings related to program abuse.

I. Assure that Adequate Risk is Borne by the Commercial Insurance Industry

Amendments to the Act in 1990 directed FCIC to assure that adequate risk is borne by the commercial insurance companies reinsured by FCIC, consistent with their ability to bear risk and the availability of commercial reinsurance. For the 1992 reinsurance year (a 12 month period that began on July 1, 1991 and ended on June 30, 1992), FCIC substantially modified its Standard Reinsurance Agreement (SRA) with the commercial insurers which participate in the program. Both the amount and the probability of losses on the part of the commercial insurers were increased in this agreement. Additional incremental changes in the amount of potential gains and losses were made for both the 1993 and 1994 SRA's.

The GAO suggests in a report entitled Crop Insurance Program Has Not Fostered Significant Risk Sharing by Insurance Companies (GAO/RCED 92-25, January 13, 1992) that the changes in the 1992 SRA are not significant enough in the area of risk bearing by the commercial insurance companies. Still, the 1992 SRA fundamentally changed the manner in which gains and losses are calculated, a subtle but effective measure to increase risk. The amount of potential loss increased, but the change in the formula increased the chances that the company would lose in years of poor experience. As a comparison, the commercial industry lost approximately $8 million in 1988 when the crop insurance program sustained a loss ratio of 2.45 primarily due to drought in the Midwest. If that experience is restated to the larger 1993 premium amounts, the loss still would have amounted to only about $10-15 million. Results from the 1993 crop year are not yet complete, but current estimates indicate that commercial insurers will sustain losses of $80-85 million although the loss ratio will be less than in 1988. The difference is caused by the SRA changes.

Some will argue that industry-wide losses of $80-85 million are not significant compared to overall program losses that may be near $900 million in 1993. Two factors bear on this issue: (1) The ability of the insurance companies to earn reserves under the SRA, and (2) The effect of losses upon an insurance company's operations in future years.

The commercial industry can bear a greater share of the losses only if there is corresponding opportunity to achieve comparable earnings in favorable years. Over the long term, the industry must achieve a satisfactory rate of return on invested capital, or it would make economic sense for participants to invest in other endeavors. The SRA must allow adequate opportunity to earn this satisfactory rate of return. It also must permit accumulation of reserves to pay losses in years that disasters strike. Under the present SRA and the conditions of actuarial soundness of the program, there is no opportunity to accumulate the reserves needed to bear a large portion of a $900 million loss.

Losses directly impact the capital structure of the companies. An insurance company leverages its capital (the term "surplus" is used by the industry) to support the volume of business that it writes. As a general rule, an insurance company is permitted by regulators to bear the risk associated with $2 to $3 of premium per $1 of surplus. The ratio of premiums to surplus may be lower for risky lines of insurance such as multiple peril crop insurance. Thus, whenever an insurance company loses a portion of its capital, its ability to accept premiums in future years is reduced by a greater amount, which in turn reduces its ability to earn profits and reserves. These factors must be considered when the ability of the industry to bear risk is evaluated, as is mandated by the Act.

As appropriate, given the factors discussed above, FCIC will evaluate (1) the need to increase risk sharing with the commercial insurance industry as the program achieves greater actuarial soundness, (2) reducing cessions to the assigned risk fund by requiring the industry to share in losses for loss ratios that exceed 5.00, (3) changing the stop loss provisions of the SRA, and (4) recruiting additional commercial insurers to participate in the crop insurance business. These changes will be made incrementally beginning with the 1995 SRA that takes effect on July 1, 1994.

J. Improve Loss Adjustment

Any actuarial and underwriting system can be affected by errors in adjustment of losses. These errors include both overpayment and underpayment of claims. Underpayment would not seem to be a factor influencing actuarial soundness, but failure to pay a loss when due will cause insured persons to question the value of the insurance and potentially reduce participation. The insurance experience also will not accurately depict the nature of the risk insured, leading to inaccuracies in future premium rates.

Some problems in loss adjustment are directly related to deficiencies in underwriting. For example, if the crop insurance policy is not clear on a particular point, the loss adjuster may find it necessary to make a determination in favor of the insured person. FCIC will undertake the following initiatives to assure high quality of loss adjustment determinations so that results are fair to insured persons and taxpayers:

- Develop uniform loss adjustment standards that clearly specify the requirements for accurate determinations.

- Continue research to improve loss adjustment methods, such as yield appraisal methods and techniques for unharvested crops, and measurement techniques for stored production.

- Strengthen the quality adjustment provisions of crop insurance contracts and develop standards to prevent abuse of production determinations when quality losses are claimed.

The contributions of these factors to achieve the 1.10 target loss ratio will be measured by a reduction in improper amounts paid on claims and a reduced error rate. The potential impact of these actions is difficult to quantify since the initiatives to improve underwriting also affect this area. These actions are ongoing. Loss adjustment standards for major crops and changes to the quality adjustment provisions are targeted for the 1995 crop year.

K. Marketing Crop Insurance

FCIC marketing efforts for 1994 will be directed by a strategic marketing plan based on information and data received from market research compiled across the country. The plan's main objectives will be to inform members of the farming community about changes in the program and to educate farmers about risk management, emphasizing the value of crop insurance to farming operations.

FCIC will conduct a year-long media campaign targeted at publications and broadcast markets with an agricultural audience.

Also, emphasis on outreach to minority farmers, traditionally under-represented in the program, will be coordinated through a Minority Outreach Marketing Plan that specifically identifies minority farmers in each of the 10 FCIC Regional Service Offices.

L. Expand Participation by Introducing New Products

Numerous ideas for products that will enhance the quality and acceptance of the crop insurance program have been suggested. These include cost of production coverage (several different concepts), dollar denominated coverage, revenue insurance, replacement cost insurance, and others. FCIC currently has contracts with the Economic Research Service to evaluate several alternatives in the context of public policy contributions, availability of data to support the concepts, assessments of producer acceptance, and other factors. FCIC proposes to continue such research and seeks comments about additional concepts that may be appropriate. Implementation of a pilot test of the best alternatives will be pursued.

M. Improve Accuracy of Other Program Variables

This section includes items that impact the program but are not easily categorized under a previous heading. These are:

- **Unit division.** A unit is a tract of land used to establish the amount of insurance and any indemnity. For example, the crop insurance policy defines a unit as all land in a county that is owned by the farmer or rented for cash and planted to the insured crop. This unit may be subdivided under certain conditions, including payment of additional premium. Generally, insured persons favor a program that gives them greater flexibility and freedom for establishing a unit. Some research indicates that size of a unit may affect losses, i.e., a unit consisting of 10 acres may have a greater loss (in relative terms) than a unit consisting of 100 acres. This research, if verified, suggests that a surcharge may be needed for small acreage units regardless of how these are formed (by dividing larger units or because this is all the land planted to the crop). FCIC will examine the research and determine if this surcharge is appropriate, both actuarially and as a public policy initiative. FCIC also will explore the potential to provide greater flexibility of unit determinations as a tool to enhance program acceptance by customers. The pricing needed to support greater flexibility must be determined before it can be implemented. Implementation of changes will be targeted for the 1996 crop year.

- **Program dates.** Program dates include sales closing, acreage reporting, cancellation, and others. Several of these dates may directly affect the actuarial soundness of the program. For example, neither the farmer nor the insurer should be able to predict the potential for loss on the sales closing date. However, a study by one university indicates that farmers may achieve better than a 50-50 probability of predicting a loss with the current sales closing date of April 15 in the Midwest. Arguments in favor of having a sales closing date as late as possible generally focus on the need to maximize sales opportunities; i.e., that interest in purchasing crop insurance is greatest as planting time approaches. In a draft report, the GAO has encouraged FCIC to close sales earlier. FCIC proposes to close sales for the 1995 crop year by 15-30 days earlier than the present dates. FCIC requests comments regarding other actions with regard to program dates that will facilitate achievement of the targeted 1.10 loss ratio.

- **Staged guarantees.** Staged guarantees reduce the amount of insurance when a crop is lost before harvest. For example, a farmer who abandons a crop within 30 days of planting might be paid only 40 percent of the amount of insurance. The concept underlying staged guarantees is investment costs; the farmer's investment is less than the total needed to produce and harvest the crop. Some believe this approach will reduce outlays for indemnities and help achieve actuarial soundness. However, in the long run its effect could be to reduce premium rates from levels otherwise needed. The impact of staged guarantees upon customer acceptance of

crop insurance may be the valid measure of this concept. FCIC specifically requests comments on this feature and assessments of its potential contribution to achieving the targeted 1.10 loss ratio.

- **De minimus yields**. This term denotes a yield below which any production is disregarded for the purpose of determining the amount of indemnity. The concept is advanced by interested parties as an equity issue--that it costs the farmer more to harvest the crop than it is worth in the market. If allowed by the program, indemnities will increase compared to the present provisions of the crop policies, which, in turn, requires higher premium rates to achieve the goal. Readers are encouraged to comment on the desirability of increasing premium rates by an amount needed to permit this feature to be included in crop insurance policies.

- **Suspension and debarment**. Inappropriate determinations and poor administration of the crop insurance program is alleged about agents, loss adjusters, and others who are involved with delivery of crop insurance. The SSN/EIN database is intended to help FCIC monitor the conduct of these persons. However, monitoring in and of itself is insufficient if there are no penalties for violations of program rules. FCIC proposes to develop clear and concise suspension and debarment procedures for agents, loss adjusters, reinsured companies and others who fail to observe the highest standards of performance in program delivery and administration.

- **Price Elections**. The GAO recommended in a 1991 report that for the major crops, FCIC set its price elections equal to the forecasts issued by the World Agricultural Outlook Board in its semi-annual estimates. These estimates correspond to the cycle used to prepare the annual budget of the United States Government. These estimates are available only twice each year. Based on a sampling of a few years, GAO stated that overall losses would be reduced if this recommendation were adopted. FCIC is committed to offering a price election that complies fully with the requirements of the law. In addition, the offer must be meaningful to farmers. FCIC requests comments regarding this recommendation and assessments by readers of its likelihood of contributing to reduced loss ratios and improved participation.

Readers are requested to identify additional issues that they believe are relevant and important to assist FCIC in its actions to manage the program to achieve the target loss ratio while maintaining or increasing participation levels.

III. MANAGEMENT ACTIONS IF SECTION II ARE NOT SUCCESSFUL

The actions identified in Section II of this document represent a major reinforcing of FCIC efforts to achieve the important goal of financial and actuarial soundness in Federal crop

insurance. FCIC believes that successful completion of these actions will meet the objective of achieving actuarial soundness as required by OBRA 93. Several years must elapse before it will be possible to observe FCIC's achievement of the objective. In the interim, attainment must be measured by realistic models of risk that adequately represent the crop insurance program. Flexibility in managing the program to attain the objective while simultaneously achieving other important policy objectives must be stressed.

Few options that do not adversely affect participation in a material manner are available in the event the actions described in this blueprint are determined to be inadequate. One option is to focus better on defining the risk that is included in the premium rates charged to current insureds. Extreme crop disasters (such as the 1993 flooding and cold, wet growing season) tend to be widespread and occur infrequently. Crop insurance is not actuarially sound in a commercial sense because the private sector cannot manage the magnitude of these risks or arrange the financing over the long periods of time needed to accumulate reserves for a major disaster. This characteristic of crop disasters argues that actuarial soundness perhaps should be measured on a basis that separates normally expected conditions from the extreme disasters. This would serve to more precisely define the risk included in the premium rates for current insureds, and the risk that should be amortized over longer time periods.

If the above is not acceptable, another action would be to limit the liability of crop insurance to specific areas and crops. This limitation could take the form of complete withdrawal of insurance in some cases, or limitations on the volume of business that would be accepted in a year for a crop or area. Commercial insurers use this process to manage their exposure to avoid concentrations geographically or by product line. Crop insurance may need the same management of its exposures rather than accepting any and all risk whenever farmers decide to enter and exit the program. This extreme action would indicate that the program was unable to completely fulfill its social and public policy responsibilities, and must be regarded as an initiative of last resort.

IV. MANAGEMENT ACTIONS IF ACTIONS IN SECTION II ARE MORE SUCCESSFUL THAN NEEDED

The greatest impediment to increased program participation will be high premium rates that might result from the actions defined in this plan. Moderation of premium rate increases will be a priority if more stringent program administration reduces the loss ratio below the target. If this occurs, experience should be examined to identify losses paid that no longer should be expected. Once the impact of those losses is eliminated from the experience, some improvement in premium rates would be anticipated. FCIC believes that the remaining management actions that have improved administration of the program or that have better defined the coverage provided to U. S. agriculture should not be relaxed because these generally represent good administration of public policy.

United States Department of Agriculture
Federal Crop Insurance Corporation
Office of The Manager
Washington, D.C. 20250

MARKET VALUE PROTECTION (MVP) PLAN

FCIC has agreed to provide reinsurance on a pilot basis for the Market Value Protection (MVP) plan, a supplemental policy developed by American Agrisurance, Inc. This action marks the first time USDA has implemented its authority under the 1990 Farm Bill to back innovative new insurance products developed by the private sector.

MVP protect farmers from becoming under-insured when the replacement cost of their crop, as measured based on futures settlement prices at harvest, rises significantly above the MPCI price election. American Agri has sold MVP to farmers since 1991 without Federal reinsurance in conjunction with Federal crop insurance as a supplemental "wrap-around" policy. However, the private reinsurance market tightened significantly because of recent catastrophic events both inside and outside of agriculture and, without FCIC backing, the product's availability will shrink dramatically for 1994 crops.

FCIC has reviewed the MVP program extensively and has determined to offer limited reinsurance offer to American Agrisurance on MVP for the 1994 crop year. The MVP approval would thus be in the nature of a pilot program with coverage limited to a dollar amount. FCIC would assess the program after the 1994 crop year in determining whether or to what extent the program should be continued for 1995. As part of this process, FCIC will determine whether it is practicable to off-set some of the price risk association with this coverage in the private options or futures markets.

Most forms of insurance, be it for a car, a house, personal property, or business inventory, provide protection based on the replacement cost of the insured article. Under MPCI as currently structured, however, insurance is based on a pre-set FCIC price for the commodity. If actual market prices change, as they did this year, gaps can result leaving the farmer over- or under-insured. For instance, if the pre-set FCIC price election per bushel for a crop is $2.60, the insured would be paid $2.60 for each bushel lost below the MPCI deductible. If the futures settlement price at harvest time is $2.75 a bushel, then a $.15 per bushel gap exists between the MPCI price and the futures settlement price.

Replacement-price policies like MVP fill this gap. In the example above, it would pay the farmer the $.15 difference on bushels lost which exceed the MPCI deductible. If prices fall, the farmer would be paid the underlying $2.60 a bushel under the basic MPCI coverage.

By approving privately-developed new insurance products like MVP, FCIC intends to encourage a process of industry innovation which has the best potential of developing useful new products to suit the needs of farmer-customers.